

Modern Business

A Series of Texts
prepared as part of the
Modern Business Course and Service



Registered Trade Mark
United States and Great Britain
Marca Registrada, M. de F.

Alexander Hamilton Institute

JOSEPH FRENCH JOHNSON

FOUNDER OF

ALEXANDER HAMILTON INSTITUTE

(1909)

AND FIRST EDITOR-IN-CHIEF

OF THE

MODERN BUSINESS SERIES

Commercial Law

By

Frank H. Sommer

Professor of Law and Dean, New York University
School of Law

AND

William F. Walsh

Professor of Law, New York University

AND

Edwin D. Webb

Professor of Law, New York University

Alexander Hamilton Institute
New York

Copyright, 1924, by Alexander Hamilton Institute

Copyright in Great Britain, 1924, by Alexander Hamilton Institute

All rights reserved, including translation into Scandinavian

Latest Revision, 1929

Made in U. S. A.

PREFACE

THE authors of this volume have set themselves the task of stating the basic principles of the law in a form in which they may be readily comprehended by one unfamiliar with the technical language of the legal craft. The task which they set themselves was not an impossible one. Had it proven impossible it would have demonstrated that the maxim of the law, "Everyone is presumed to know the law," or more accurately, "Ignorance of the law excuses no man," had no foundation on which to rest.

If it is true that business men need to understand the basic principles of the law, the proposition that general knowledge of the underlying principles and processes of business should form part of the equipment of those who aspire to a part in shaping and administering the law is equally true. It has, however, been slow to gain general acceptance. It was, and in large measure still is, the accepted theory that a program made up exclusively of "cultural" subjects, affords the most effective foundations for the study of the law with a view to its practice as a profession. In such a program the underlying principles and processes of business, of course, find no place. Signs, however, are not wanting of a growing realization of the fact that because so large a part of the law is made up of principles relating to business

transactions, general knowledge of the essential principles and processes of business should form part of the armory of the lawyer.

If, on the one hand, general knowledge of business comes to be a requirement in the preliminary training of the lawyer, and if, on the other hand, general knowledge of the broad principles of law comes to be recognized as an essential part of the equipment of the business man, a common meeting ground for the two will exist. On this common meeting ground the interrelated and interdependent problems of business and law may most advantageously be worked out.

On it, too, the causes of the increasing dissatisfaction of business men with the law as it relates to business, and with its administration, may be uncovered and subjected to calm analysis in the light of the requirements of business, and the essential characteristics and requirements of rules of law.

Out of such a process of joint uncovering and analysis, which simply involves a return to the practices of an earlier day, a body of law relating to business may be expected to be developed in which inconsistency with business practices, which are the results of protracted experience, may be reduced to a minimum.

To that end this volume is a modest contribution and to its furtherance the series of which this volume is a part, serves.

FRANK H. SOMMER.

TABLE OF CONTENTS

CHAPTER I

SOURCES AND CLASSIFICATIONS OF LAW

SECTION	PAGE
1. Introductory	1
2. Nature of Law	1
3. Law and Justice	3
4. Classifications of Law	4
5. The Common Law	4
6. Equity, Its Origin	5
7. Development of Equity	6
8. Illustrations, Specific Performance	7
9. Injunction	8
10. The Jury at Law and in Equity	10
11. Consolidation of Law Courts and Equity Courts	10
12. Varying Significance of the Term "Common Law"	10
13. The Common Law of the States of the United States	11
14. Responsiveness of the Common Law to Changed Conditions	11
15. Legislation	14
16. Constitutional Law	15

CHAPTER II

CONTRACTS—THE OFFER

1. Contracts, the Foundation of Business Law	18
--	----

SECTION	PAGE
2. What the Law of Contracts Includes	18
3. Types of Contracts	19
4. Essentials of a Simple Contract	20
5. Mutual Assent, How Expressed	21
6. Nature of Offers and How Made	22
7. Preliminary Negotiations and Advertisements	23
8. Preliminary Agreement to be Followed by Written Contract	24
9. Auction Sales	25
10. Advertisements for Bids on Public Works	25
11. Offers Must be Communicated	26
12. Rewards	26
13. Offers by Mail	27
14. Indefinite Offers and Promises	27
15. Indefiniteness as to Price, Services or Goods	29
16. Offers Implied from Acts or Conduct	29
17. How Offers are Terminated before Acceptance	30
18. Termination of Offers by Rejection	32
19. Rejection by Mail or Telegraph	32
20. Revocation of Offers	33
21. Revocation of Offers by Advertisement	34
22. Revocation of Offers to Pay for Acts	34
23. Termination of Offers by Death or Insanity	35
24. When Offers are Irrevocable	36

CHAPTER III

CONTRACTS—THE ACCEPTANCE

1. Acceptance of Offers	38
2. The Acceptance Must not Modify the Offer	39
3. Acceptances by Mail, Telegraph or Telephone	40
4. Effect of Actual Receipt of Acceptance before Offer Lapses	41

CONTENTS

ix

SECTION

PAGE

5.	Acceptance of Offer Calling for an Act, not a Promise	41
6.	Acceptance Implied in Fact	42
7.	Effect of Acceptance of Writings	43
8.	Signing or Acceptance of Writings by Illiterate Persons	43
9.	Acceptance by Silence	44
10.	Mistake of the Parties as to Terms of the Contract	44

CHAPTER IV

CONTRACTS—CONSIDERATION

1.	General Nature of Consideration	46
2.	Consideration, a Benefit to the Promisor or Detriment to the Promisee	46
3.	Consideration in Unilateral Contracts	47
4.	Consideration in Bilateral Contracts	48
5.	A Promise to Do Something Which the Promisor is Already Bound to Do is not a Valid Consideration	48
6.	Contingent Promises are Valid as Consideration for Counter-Promises	50
7.	Contracts under Seal	50
8.	Gratuitous Conditional Offer Distinguished from Offer Calling for an Act as Consideration	51
9.	Consideration may be of Benefit to a Stranger	52
10.	When Payment of or Giving of Security for a Debt is a Valid Consideration	53
11.	Extension of Time to Pay a Debt	53
12.	Payment in Full Settlement of Claims Uncertain as to Amount or Disputed	54
13.	Special Inducements to Fulfil Existing Contracts	54

SECTION	PAGE
14. Promise to Perform Existing Contract with Third Person	55
15. Doing or Promising to Do What the Party is Bound by Law to Do is not Consideration .	56
16. Past Consideration	56

CHAPTER V

CONTRACTS—PARTIES AND FORM

1. Validity of Contracts	58
2. Infant's Contracts	58
3. Contracts for Necessaries	59
4. Insane Persons as Parties to Contracts	61
5. Acts of Adjudged Lunatic Void	62
6. Drunkenness	62
7. Married Women	63
8. Contracts Made for the Benefit of Third Persons .	63
9. Third Person as Sole Beneficiary	64
10. Promisee and Third Person Benefited	64
11. Assumption of Mortgage Debt	65
12. When Contracts Must be in Writing	66
13. Statute of Frauds	67
14. Contracts not to be Performed within a Year .	68
15. Contracts for Indefinite Periods	68
16. Contracts not to Compete	69
17. Method of Performance	69
18. Contracts in Consideration of Marriage	70

CHAPTER VI

CONTRACTS—PERFORMANCE

1. Conditions in Contracts in General	72
---	----

CONTENTS

xi

SECTION	PAGE
2. Express Conditions	73
3. Conditions Implied in Fact	73
4. Conditions Implied in Law	74
5. Performance Prevented by Promisor	75
6. Waiver of Performance of Conditions	76
7. Waiver before Time for Performance	76
8. Waiver after Breach of Condition	77
9. Conditions in the Sales of Goods	78
10. Other Illustrations	79
11. Conditions Requiring Architects' Certificates	80
12. Conditions as to Time of Payment of a Debt	81
13. Substantial Performance	81
14. Conditions Implied by Law in Bilateral Contracts	82
15. Failure of Performance by one Party Relieves the Other from His Promise	83
16. When Order of Performance is not Indicated	84
17. Concurrent Conditions	84
18. Tender and Readiness and Willingness to Perform	85
19. Impossibility of Performance of Conditions not Due to Fault of the Plaintiff	86
20. Part or Substantial Performance	87
21. Time of Performance—When Time is of the Es- sence	88
22. Contracts of Sale, Time is of the Essence	89
23. Time is of the Essence in Other Cases	89
24. Severable or Divisible Contracts	90
25. Effect of Prospective Unwillingness or Inability to Perform	91

CHAPTER VII

CONTRACTS—ASSIGNMENT AND DISCHARGE

1. Nature of Assignment of Contracts	93
--	----

SECTION	PAGE
2. What Contractual Rights may be Assigned . . .	94
3. How Far Future Contractual Rights may be Assigned	95
4. Assignments Contrary to Public Policy . . .	96
5. Assignment of Executory Bilateral Contracts .	96
6. Effect of Express Prohibition of Consent to Assignment	97
7. Distinction between Assignment and Order, Drafts and Checks	98
8. Form of Assignments	98
9. Defenses Which the Obligor may Set up against the Assignee	99
10. Discharge of Contracts	100
11. Release of Contracts	100
12. Rescission by Parol	101
13. Accord and Satisfaction	102
14. Attempted Satisfaction of Disputed Claim by Check	103
15. Accounts Stated	104
16. Novation	105
17. Rescission for Breach of Contract	106
18. Cancellation	106
19. Alteration	107
20. Discharge of Contracts by Merger	107
21. Impossibility of Performance	108

CHAPTER VIII

NEGOTIABLE INSTRUMENTS

1. Origin of Negotiable Instruments	112
2. Negotiability	113
3. Negotiability of Promissory Notes	115
4. Form of Negotiable Instruments	116

CONTENTS

xiii

SECTION	PAGE
5. Formal Requisites of Negotiable Instruments . . .	117
6. Instrument Must be Written and Signed by Maker	118
7. Unconditional Promise	119
8. Certainty as to Amount	120
9. Time Must be Fixed or Determinable	121
10. Parties Must be Identified	121
11. Collateral Notes	122
12. Omissions and Blanks	123
13. Interest	125
14. Consideration	126

CHAPTER IX

PARTIES TO NEGOTIABLE INSTRUMENTS AND THEIR OBLIGATIONS

1. Liability of Maker	128
2. Kinds of Indorsement	129
3. Blank Indorsement	130
4. Special Indorsement	130
5. Restrictive Indorsement	131
6. Indorsement without Recourse	133
7. Conditional Indorsement	133
8. Liability of Indorser	133
9. Liability of Accommodation Indorser	134
10. Other Provisions as to Indorsement	136
11. Necessity of Presentment for Payment	138
12. What Constitutes Sufficient Presentment	139
13. Notice of Dishonor	141
14. Within What Time Must Notice of Dishonor be Given?	143
15. Protest	144

CHAPTER X

BILLS OF EXCHANGE

SECTION	PAGE
1. Nature	146
2. Liability of Drawee	147
3. Liability of Drawer	148
4. Rights of Holder of a Negotiable Instrument	150
5. Defenses	152
6. Incapacity	153
7. Illegality	154
8. Usury	155
9. Forgery	156
10. Personal Defenses	158
11. Lack of Consideration	159
12. Payment	160

CHAPTER XI

CHECKS AND OTHER INSTRUMENTS

1. Nature of a Check	163
2. Relation between Bank and Depositor	164
3. Rights and Liability of the Drawer of a Check	165
4. Rights and Liabilities of Holder of a Check	167
5. Certified Checks	169
6. Bill of Lading	171
7. Coupons	172
8. Certificate of Deposit	173
9. Letter of Credit	173
10. Money Orders	174
11. Stock Certificates	174
12. Trade Acceptances	176
13. Warehouse Receipts	176

CHAPTER XII

SALES—STATUTE OF FRAUDS

SECTION	PAGE
1. Principal Aspects of the Law of Sales	178
2. Provisions of the Statute	178
3. Sales and Executory Contracts to Sell	179
4. Contracts to Sell Distinguished from Contracts for Work and Labor	180
5. What is Included within "Sales of Goods"	181
6. Provision as to Value of the Goods	182
7. Acceptance and Receipt of Part of the Goods	182
8. Part Payment under the Statute	183
9. The Memorandum in Writing	184

CHAPTER XIII

SALE—PERFORMANCE—RIGHTS AND LIABILITIES OF PARTIES

1. Delivery and Payment of the Price	186
2. Time and Place of Delivery	186
3. Delivery to a Common Carrier	187
4. Delivery of a Greater or Less Quantity	188
5. Examination of the Goods by the Buyer	189
6. Transfer of Title	190
7. Goods Shipped C. O. D.	191
8. Reservation of Title for Possession by Sellers	191
9. Risk of Loss	192
10. Goods Shipped under Bill of Lading	192
11. Sale by Person not having Title to Goods Sold	193
12. Conditional Sale	193
13. Sale with Retention of Possession by Seller	194
14. Express Warranties in Sales	195

SECTION	PAGE
15. Obvious Defects—Inspection	195
16. Implied Warranty of Title	196
17. Implied Warranty of Quality	197
18. No Warranty Broken When Buyer Gets What He Contracted For	199
19. Warranty That Food Sold for Immediate Con- sumption by a Dealer is Fit	200
20. Merchantability	200
21. Sale by Sample	200

CHAPTER XIV

BAILMENTS AND CARRIERS

1. Nature of a Bailment	202
2. When the Bailed Goods Belong to a Third Per- son	202
3. Gratuitous Bailments	203
4. Bailments not Gratuitous	204
5. Pledges	205
6. Storage or Warehouse Bailments	206
7. Bailments with Innkeepers	207
8. Liability of Common Carriers	207
9. Acts of God	208
10. Public Enemies	208
11. Damages Due to Inherent Character of Goods Shipped	209
12. Carriers' Liability for Delay	209
13. Limiting Liability by Express Contract	209
14. Provisions Restricting Damages to a Fixed Sum	210

CHAPTER XV

AGENCY—CREATION AND TERMINATION

1. Nature of Agency	212
-------------------------------	-----

CONTENTS

xvii

SECTION	PAGE
2. Agency Created by Express Appointment	213
3. Competency of the Parties	213
4. Unincorporated Associations as Principals	214
5. Joint Agents	214
6. Form of Appointment, Writing and Seals	215
7. Creation of Agency by Ratification	216
8. Requisites of Ratification	216
9. Form of Ratification	218
10. Right to Withdraw before Ratification	218
11. Effects of Ratification	218
12. Agency Arising by Estoppel	219
13. Agency to Collect on Bond and Mortgage from Possession of the Documents	221
14. Termination of Relation of Principal and Agent	222
15. What Constitutes Revocation	222
16. Notice of Revocation	223
17. Revocation by Operation of Law	223
18. Death of Either Party Terminates the Agency	223
19. Irrevocable Agency	224

CHAPTER XVI

PRINCIPAL, AGENT AND THIRD PERSON

1. Obligations of Principal to Agent	226
2. Real Estate Brokers' Commissions	227
3. Effect of Revocation of Agency on Compensation	227
4. Discharge of Real Estate Brokers	228
5. Compensation Where Agent Acts for Both Sides	229
6. Illegal Services	230
7. Reimbursement and Indemnity	231
8. Obligations of Agent to Principal	232
9. Delegation of Authority by Agent to Others	234
10. Sub-Agents	235

SECTION	PAGE
11. Liability of Gratuitous Agents	236
12. Liability of Principal to Third Persons	237
13. General Managers or General Agents	238
14. Authority of Agents to Sell	238
15. Authority of Agents to Buy	239
16. Factors	239
17. Brokers	240
18. Auctioneers	240
19. Lawyers	241
20. Rights and Liabilities of an Undisclosed Principal	241
21. Is the Agent's Misrepresentation Legal Fraud?	242
22. Exceptions to Doctrine of Undisclosed Principal	243
23. Notice to Agent is Notice to Principal	244

CHAPTER XVII

PARTNERSHIP

1. Legal Nature of Partnership	246
2. Partnership and Joint Ownership	247
3. Other Forms of Organization	249
4. The Contract of Partnership	250
5. Holding out as a Partner	251
6. Sharing in Profits not Always Partnership	252
7. Firm Capital	253
8. Partnership Property	253
9. Partnership Real Estate	254
10. Partner's Interest in Firm Property	255

CHAPTER XVIII

RIGHTS AND LIABILITIES OF PARTNERS

1. Good Faith	258
-------------------------	-----

CONTENTS

xix

SECTION	PAGE
2. Management of the Partnership	259
3. Application of Firm Assets	259
4. Enforcement of Obligations among Partners	261
5. Power of Partner to Bind Firm by Contract	261
6. The Scope of the Business	262
7. Instruments under Seal	263
8. Fixed Property	264
9. Individual Debts	265
10. How a Partner's Authority is Shown	266
11. Firm Bound by Wrongful Act of Partner	267
12. Extent of Partner's Liability	268
13. Rights of Firm Creditors	269
14. Individual Creditors	270
15. Dissolution	271
16. Final Accounting	272
17. Limited Partnership	274

CHAPTER XIX

SURETYSHIP AND GUARANTY

1. What Constitutes Suretyship and Guaranty	276
2. Contract between Creditor and Surety	277
3. How Defenses of the Principal Debtor Affect the Surety's Contract	277
4. Discharge of Surety by Payment or Release of Principal Debt	278
5. Extension of Time by Creditor Discharges Surety	279
6. Reservation of Right to Hold Surety Prevents his Discharge	280
7. Surrender of Collateral Security Discharges Surety Pro Tanto	280
8. Variation or Alteration of Principal Debtor's Con- tract	282

SECTION

PAGE

9.	Tender of Payment and Rejection by Creditor	283
10.	Failure of the Creditor to Sue Debtor	284
11.	Notice to Surety of Debtor's Default	284
12.	Fraud or Duress by Debtor or Creditor to Surety	284
13.	Termination of the Contract	285
14.	Rights of the Surety-Reimbursement	286
15.	Surety's Right of Contribution	286
16.	Contribution between Sureties for Different Sums	287
17.	The Statute of Frauds	287

CHAPTER XX

REAL PROPERTY—DEEDS AND MORTGAGES

1.	Real Estate and Personal Property	289
2.	Fixtures	290
3.	Land Ownership	292
4.	Deeds and Conveyances	293
5.	Different Parts of a Deed	294
6.	Covenants of Title	295
7.	Mortgages	296
8.	Improvements by Mortgagee	298
9.	Rights and Obligations of Mortgagor	299
10.	Equitable Mortgages	300
11.	Illegal Mortgages	301
12.	Assumption of Mortgage by Purchaser of Mort- gaged Property	302
13.	Foreclosure of Mortgages	304

CHAPTER XXI

REAL PROPERTY—LEASES

1.	Landlord and Tenant	307
----	-------------------------------	-----

CONTENTS

XXI

SECTION

PAGE

2.	Tenancies from Year to Year and from Month to Month	309
3.	Tenancies at Will	311
4.	Tenancies under a Void Parol Lease	311
5.	Covenants in Leases	312
6.	Waste	313
7.	Surrender of Leases	314

CHAPTER XXII

PERSONAL PROPERTY

1.	Aspects of Personal Property	316
2.	Possession and Ownership	316
3.	Lost Property	317
4.	Lost Chattels Found on Land Privately Owned	317
5.	Misplaced Chattels	318
6.	Possession of Tenant and Bailee	319
7.	Adverse Possession	321
8.	Accession	321
9.	Confusion	322
10.	Voluntary Transfer of Title to Chattels	323
11.	Common Law Liens on Chattels	323
12.	Artisans' Liens and Liens of Warehousemen	324
13.	Incidents of Common Law Lien	325
14.	General or Commercial Liens	325

CHAPTER XXIII

FIDUCIARIES

1.	Nature of the Relation	327
2.	Trust Property	329

SECTION	PAGE
3. Rights and Duties of Trustee	331
4. Investments by Trustees	333
5. Other Duties of a Trustee	334
6. Relations of Third Persons to the Trust	335
7. Rights of Beneficiaries	337

CHAPTER XXIV

QUASI-CONTRACTUAL OBLIGATIONS

1. Nature	340
2. When the Obligation Arises	343
3. Mistake	343
4. Mistake as to Existence of a Contract	344
5. Mistake as to Identity of Dealer	345
6. Mistake as to Subject of a Contract	347
7. Mistake as to a Material Fact	348
8. Mistake of Law	350
9. Other Cases of Retaining Benefits without Making Compensation	350
10. Illegal Contract	352
11. Contracts Void because of Statute of Frauds	353
12. Benefits Voluntarily Conferred without Contracts	355

COMMERCIAL LAW

CHAPTER I

SOURCES AND CLASSIFICATIONS OF LAW

1. *Introductory.*—The proposition that a general knowledge of the basic principles of the law should form part of the equipment of business executives, and of those looking forward to executive positions, has been stated so often that it has become trite. It has not, however, come to be so commonly acted upon as to make its repetition unnecessary. The basis upon which the proposition rests is obvious; it is these principles that determine the rights and obligations which result from business transactions. Without general knowledge of them, a man entering upon business negotiations is in much the position of the navigator adrift upon the high seas without compass or chart.

2. *Nature of law.*—Not even Robinson Crusoe living alone upon his unknown island possessed entire freedom. He could take what he found and was under obligation to no man, government or potentate. Yet there were restrictions upon his conduct. Nature permitted him to live only upon condition that he conform to her laws of life. When the man Friday ap-

peared Crusoe could enjoy his companionship only at the price of sharing with him the products of the island. If other humans had joined them the addition of each one to the community would have still further restricted the liberty of the first comers. Concessions would have to be made to enable the new comers to gather and keep for use necessary food and shelter. The other members of the group would have to concede to one who caught a fish or built a hut the privilege of keeping and using it. The idea of individual ownership, the idea of property, would necessarily come into existence by the common consent of the community. Inevitably, other customs would grow up by common consent for they would be found necessary to the continued life of the community. If there was only one spring of fresh water it would be necessary to allow each individual to use the water. And it would be necessary to the continued existence of the group that no member should be permitted to monopolize the water of the spring or defile it. It would be so vital to the welfare of the community to preserve the purity of the water and freedom of access to the spring that death would be regarded as proper punishment for one who defiled or monopolized it. The common will of the community thus expressed would then become the *law* of the island. Increasing population would necessitate more and more complex restrictions upon the liberty of the individuals in order to enable them all to live together in peace. It is obvious

therefore that in human relationships law is in the nature of a restriction upon the liberty of the individual imposed by the will of the whole community or of a particular group in the community sufficiently numerous or aggressive or powerful to enable them to impose their will upon the others. Its nature remains the same when the community expands into cities, states and nations. The law is still the expressed will of the strongest elements of the population limiting the freedom and subordinating the privileges of the individual in the supposed interest of the whole.

3. *Law and justice*.—Law, in the sense here considered, consists of the aggregate of the rules recognized, applied and enforced by courts of justice.

It has for its subject matter the legal rights and duties of men, which legal rights and duties it defines and delimits.

Its object is to establish justice.

Justice has been declared to be “the set and constant purpose to give to every man his due,” and the precepts of the law, have been asserted to be these:—“To live honorably, to injure no one, and to give to every man his due.”

Legal and moral justice are not one, though legal justice attempts to realize moral justice. Many matters within the realm of moral justice are left untouched by legal justice because of the conviction that interference thru the law would be productive of more harm than good.

An illustration may be found in the fact that while the law has defined the relation of landlord and tenant, it has not, until recently, attempted to hold the landlord to exacting no more by way of rent than he morally ought to exact. However, when not long since in the shortage of housing facilities it became a matter of general public conviction that more good than harm would result from interference, the field of the law was extended by the enactment of statutes in New York and elsewhere limiting the landlord's power of exaction.

4. *Classifications of law.*—For convenience we classify the law: with reference to the *mode of expression*, into written and unwritten law, including constitutions, statutes, ordinances, charters, proclamations, treaties, on the one side, and common law and equity, on the other; with reference to the *subject matter*, into public law, private law, international law, constitutional law, municipal law, criminal law, civil law, admiralty law, corporation law, commercial law, and so on. Before we proceed with our discussion of those parts of the law which most directly affect the business man it will be well to notice very briefly a few of the matters involved in this classification.

5. *The common law.*—The common law is the system of law which developed in England thru the decisions rendered in the courts. These decisions declared general rules and applied them in determining the controversies before the courts. These general

rules so applied, rested in the beginning upon customs prevailing in the community; they crystallized such customs and gave them legal force. The decisions formulating and applying these general rules, began at an early date to be recorded and preserved in "reports." It became the practice of the judges to turn to these reports to determine whether a problem newly presented to them had been previously considered. Out of this practice grew the rule that a decision in an earlier case should, in general, govern and control, when applicable, the determination to be made in a later case.

The common law, therefore, finds its source (a) in prevailing community customs and (b) in precedents.

6. *Equity, its origin.*—In the time of Edward I, the common law in its development failed to meet the needs occasioned by social and economic changes. This failure was due to the conservatism of the judges of the King's courts administering the common law and to the limiting effect of the procedure thru which their jurisdiction to afford relief in a given case was acquired and governed. A practice then arose of appealing directly by petition to the King for relief, where the common law afforded no remedy, or a remedy regarded inadequate. This practice was the result of the theory that the King was the "Fountain of All Justice." The King considered the petitions so addressed to him and when in his judgment relief was demanded, granted it as a matter "of Grace." In the course of time the King

in specific instances delegated the power of considering and acting upon such petitions to his Chancellor, until finally Edward III by a general writ vested the power in the Chancellor. In this manner the Court of Chancery exercising its jurisdiction upon principles of "Equity and good conscience" originated.

Equity, therefore, grew out of the need of providing legal relief where the common law as developed and administered by the King's courts, either afforded no relief or relief that was inadequate or incomplete.

7. *Development of equity.*—During the formative period of equity the Chancellor determined each new case coming before him according to what his sense of "natural justice" and "good conscience" required. Equity consequently came to consist of "such principles of received [accepted] morality as were applicable to legal questions and commended themselves" to the Chancellor.

The judgment of the Chancellor, however, was influenced by the principles of the Roman and Canon law with which as an ecclesiast he was acquainted.

In the passing years thru the giving effect in later cases to the precedents established in earlier cases, equity developed into a body of rules limiting the jurisdiction of the Court of Chancery substantially as effectually as the rules of the common law limited the jurisdiction of the King's courts of common law.

Many of these rules have found expression in maxims, as for instance, "Equity suffers not a right to be without a remedy," "He that will have equity

done him, must do it to the same person"; "He that hath committed Iniquity, shall not have Equity"; "Equity relieves against Accidents"; "Equity suffers not advantage to be taken of a penalty or forfeiture, where compensation can be made"; "Equity prevents mischief"; "Equity prevents multiplicity of suits"; "Where Equity is equal, the Law must prevail."

8. *Illustrations, specific performance.*—How equity complements and supplements law may be shown by example.

If a merchant contracts to sell 1000 pair of shoes to you for \$5000, and you tender him the price, but he refuses to perform his promise and deliver the shoes to you, what remedy is available to you? At law you may sue him for damages for breach of the contract and recover judgment for a sum representing the difference between the price you promised to pay and the amount you would be obliged to pay in purchasing like shoes in the open market. No other form of remedy could be afforded you thru the law as distinguished from equity—the law here is confined to awarding damages.

Equity is not so limited in the manner of relief afforded. If the case were appropriate for granting such relief, equity might decree that the merchant specifically perform his promise and deliver the shoes to you. Under the facts assumed, however, equity would not afford such relief, since the remedy at law, thru the award of damages would be regarded as

adequate, because the purchase price and damages awarded would enable you to effect a purchase in the open market and thereby put yourself substantially in the position which would have been yours if the merchant had fulfilled his promise.

If, however, the contract was one to sell to you personal property not readily obtainable in the open market, or personal property having unique qualities, as shares of capital stock of a corporation making up the controlling interest, or a painting by a noted artist, the situation would be different.

In these cases the remedy afforded at law thru an award of damages would not be regarded as adequate, and you might proceed in equity to secure a decree requiring the delivery to you of the shares or painting.

9. *Injunction*.—Again, assume that you purchase a business as a going concern and the seller promises that he will not engage in the same business thereafter within the territory over which the good-will of the business extends, and that the seller in breach of his promise is preparing to re-enter the business, what course is open to you?

At law, you must await the seller's actual re-engagement in the business. Until then he has not violated the contract, and without such violation no right to sue at law exists. On such violation you may sue him at law for damages.

It requires no argument to carry conviction that the remedy so granted is not adequate; the essential

purpose contemplated when you took the promise was to prevent competition. Equity here meets the inadequacy of the remedy at law by enjoining the seller from re-entering the business and commanding him to refrain from a breach of his promise.

If thru fraudulent representations made to you by another you deliver him your promissory note payable to his order, the law simply affords you an opportunity to defend a suit that may be brought against you on the note. If such suit is brought by the one to whom you delivered the note, you may defeat it by setting up his fraud in defense. If, however, before the due-day of the note he has transferred the title and possession of the note to another, for value and that other had no notice of the fraud, and suit is brought against you by such holder, the fraud perpetrated upon you by the payee of the note will not avail you as a defense, for the one bringing the suit is the so called "purchaser for value without notice." Here again it is apparent that the remedy afforded by the law is inadequate.

In equity, when you discover the fraud you may sue to enjoin the negotiation and transfer of the note by the payee to another and to require the surrender of the note; the relief that is afforded here thru equity is preventive.

Illustrations might be multiplied.

In the case of trustees, administrators and other fiduciaries who fail in the discharge of their duties, equity affords a remedy by requiring complete ac-

counting, so too as between co-partners. Such relief the law, confined in general to awarding damages, cannot afford.

10. *The jury at law and in equity.*—In suits at law the facts in controversy are determined by the verdict of a jury. In suits in equity the facts are determined by the court. If a court of equity is confronted by a complex fact problem, it may “frame an issue,” stating the question of fact to be determined, and send this issue into a court of law for the purpose of taking the verdict of a jury thereon. The verdict is, however, only advisory. It in no wise binds the court of equity, which court may accept or wholly or in part reject it.

11. *Consolidation of law courts and equity courts.*—While law and equity were administered in the beginning in many of the States, as in England, thru separate and independent courts, this is no longer the rule, but rather the exception. One court now administers both law and equity.

12. *Varying significance of the term “common law.”*—The term “common law” is frequently used in other senses than that in which we have used it above in contradistinction to “equity.” The systems of law prevailing in the countries of western Europe were derived from the law of the Roman empire, which is called the “civil law.” The term “common law” is also frequently used to denote the entire law of England, written and unwritten, in contradistinction to the civil law.

13. *The common law of the States of the United States.*—Our colonial ancestors coming from England brought with them the general principles of the common law, including equity, and the statutory law as well, in so far as the same was applicable to the new conditions. This body of law is generally referred to as the common law of the States of the United States and prevails in practically all of them except as later enacted statutes have effected changes therein. Louisiana was settled by the French and retained the civil law: Florida, Arizona, and New Mexico, altho settled by the Spanish and still showing the influence of Spanish law, have adopted by statute the common law as the basic law of those states.

14. *Responsiveness of the common law to changed conditions.*—There is a common impression that the law, insofar as it is the result of judicial decision, is essentially static. There is a wide-spread belief that it does not develop and expand as social and economic conditions change. The necessarily brief comment on the history of some of the rules of the common law in the pages following makes it clear that in general this impression and this belief are without foundation. The fact is the contrary. Pride in the common law rests upon its flexibility as a system and its capacity to grow, expand and contract as the requirements of changed conditions may from time to time demand.

This quality of the common law is illustrated by the rise and development of the common-law rules

relating to the problem as to what contractual restraints of trade are enforceable. At first this body of rules, in one of its applications, condemned all attempts to impose a restraint upon trade without limitation of the territory within which such restraint should operate. Step by step the restriction thus imposed upon the power to contract freely has been waived as trade and commerce have expanded, as means of communication and transportation have been improved and new means provided,—as the peoples of the world have been brought closer to one another. Finally, as it stands, it admits of a world-wide restraint when such restraint is reasonably required in the protection of the legitimate interest of the one for whose benefit the restrictive promise was made.

The flexibility of the common law has admitted of extending the rule which required, and still requires inn-keepers, and common carriers whose vehicles were horse drawn, to render their services without unreasonable discrimination and upon reasonable charges so that now that rule applies to those engaged in operating new means of transportation—railroads, street railways, and the like—and, in fact, to all forms of so-called public utility services. These facilities came, as to their operation, within the reason of the rule because of the immediate relation between the manner in which they are conducted and the general welfare.

Another example of this quality of the common

law is the fact that it has admitted the passing of the shoer of horses, out of the class subject to these restrictions upon the withholding of service and exaction of compensation at will, into the class entitled to serve or withhold service and to exact compensation on an unrestricted contractual basis. This change was coincident with the rise of means of transportation not requiring the use of the horse and with the consequent lessening of the specific social interest in the welfare of the horse and in the form of transportation in which the horse is an essential part.

It is true that the advance of the common law to meet new conditions has at times been halting and slow and at other times has come to a dead stop along certain lines. This, however, has not been due to a lack of capacity to develop and advance, inherent in the common law. It has rather been owing to the characteristic caution and conservatism of those trained in the law, to the retarding force of tradition and to a failure to appreciate clearly the requirements of the new order of things.

In instances, which space will not admit of enumeration, the pause or stop has been fully justified, and the task of making a change and of marking out the lines of advance has been wisely left by the courts to the legislatures. Such justification is found in the fact that courts cannot, as can legislatures, give their action in changing, expanding or restricting a rule of law prospective effect only—projecting the consequences of the change into the future alone.

The instances most frequently pointed to as evidencing the non-progressive character of case-made law occur in the branches relating to property and contract. Here certainty and stability in the law are prime requisites in the protection of business interests. It is this consideration that has, and will ever, act as a caution sign, for it may well be that the disturbance of interests, which would be caused by changes operating retrospectively as well as prospectively, might work injustice outweighing the possible advantages.

These comments should be kept in mind in reading the following chapters. If, with respect to a rule stated as representing the law as it now exists, question arises in your mind as to whether it comports with present-day needs and prevailing practices, and you answer the question, after careful consideration, No,—it may well be that in the passing years the courts will make like answer and the rule then reappear in the modified and altered form required by these needs and practices.

15. *Legislation.*—Attention has been directed in some detail to law as the product of judicial decision—so called “judge-made law”—made up of the aggregate of the rules of the common law and of equity. This is the “unwritten law,” which is so designated because it was originally without written form.

Attention must now be directed to the “written law,” limiting ourselves, however, to legislative enactments, statutes, and constitutions.

The primary distinction between law, the product of legislation, and, law, the product of judicial decision, is found in the fact that legislation, in general, prescribes a rule in advance to regulate future action, whereas judicial decision declares a rule as pre-existing and gives it effect in disposing of the case before the court.

Legislation is given prospective effect only—is operative in the future alone—unless the statute specifically provides that it shall operate retrospectively and extend to past transactions as well.

Courts on the other hand in disposing of a case before them *declare* the law to have been in existence already and apply it. The consequence is that the law so declared and applied covers transactions and events in the past.

Legislation may change or abrogate the rules of common law and equity, at the will of the legislative body. The power of legislation in this respect is, of course, subject to such limitations and restrictions as may be imposed upon it by the provisions of the Constitution of the United States or of the particular state concerned.

16. *Constitutional law*.—The constitution of a state or nation comprises the fundamental principles upon which the government is founded. It may be unwritten, as in England, or written, as in the United States.

The United States government possesses the

powers delegated to it by the states in the adoption of the Constitution of the United States. It possesses no other powers.

All powers not so conferred upon the United States, by the constitution, and not prohibited by it to the States, are expressly reserved to the states respectively.

This constitution is the paramount law of the land.

Article VI of the constitution expressly provides that, "This Constitution and the laws of the United States which shall be made in pursuance thereof, and all treaties made or which shall be made, under the authority of the United States, shall be the supreme law of the land; and the judges in every state shall be bound thereby, anything in the constitution or laws of any state to the contrary notwithstanding."

Each state in the union has a written constitution which has been adopted by the people of the state in the exercise of their sovereignty.

Every law enacted by congress must be authorized by and must conform to the constitution of the United States; every state constitution must conform to the federal constitution; and every law passed by a state legislature and act done by a state official must conform to both the federal constitution and the constitution of the state.

Constitutional law is that branch of law which deals with the interpretation and enforcement of constitutions.

REVIEW

Classify the law and trace its development.

Explain the meaning of equity and its origin.

Define specific performance and give an illustration of it.

Tell what is meant by injunction. Illustrate.

Cite instances indicating how the law has kept pace with business.

NOTE: The review questions thruout this Volume are for the personal convenience of the reader in testing his understanding of the chapter. It is not necessary or desirable for subscribers to submit written answers to the Institute except in a case where they may feel uncertain as to their grasp of the question under consideration.

CHAPTER II

CONTRACTS—THE OFFER

1. *Contracts, the foundation of business law.*—All modern business is based on the fundamental principles of contract. The business man must understand these fundamental principles if he is to understand the legal basis of any business relations. The law of business, made up of the different branches of the law discussed in this volume, is founded on these basic doctrines of contractual liability. It is clear, therefore, that we must start with a careful and thorough study of contract law.

2. *What the law of contracts includes.*—Contracts are those promises which the law enforces. Promises which give rise to no obligation at law are not contracts. The law of contracts is divided into three general parts:

(a) The making of contracts, consisting of the rules of law fixing the requirements that must exist in order that a contract may arise

(b) The performance of contracts, made up of the rules of law which govern the parties in the actual carrying out of the contract

(c) The discharge of contracts, or the ending of the contractual relation, comprising the rules of law by which an existing contract may be brought to an end, as by performance, release, or novation.

These general divisions of the subject will be taken up in the order stated above.

3. *Types of contracts.*—Contracts are divided into (a) simple contracts, which include the great mass of business contractual transactions made by word of mouth or in writing without a seal, and (b) written contracts under seal. Contracts under seal, sometimes called specialties, were first made in the twelfth and thirteenth centuries as leases of land to tenants for a term of years, and have always been enforced because of the formality with which they were made or executed. Simple contracts came into the law some centuries later to meet the demands of a slowly developing business life among the people.

Another important division of contracts is into bilateral contracts and unilateral contracts. A bilateral or two-sided contract is one in which each party promises to do something, as where Jones promises to mow Smith's lawn, and Smith promises to pay him a dollar for doing so. A unilateral or one-sided contract arises where only one party promises to do something in return for the act of the other, the other party making no promise, as where Smith promises to pay Jones a dollar if he will mow Smith's lawn. In this latter case no contract arises until the act, the mowing of the lawn, is completed; Jones has then accepted Smith's proposition which becomes a legal contract by Jones' act of acceptance. What Smith wanted was Jones' act, not his promise. This dis-

tion is fundamental, as will clearly appear when we discuss offer and acceptance.

It is a common thing to speak of contracts as *executed* and *executory*. An *executed* transaction, as for instance a sale completely performed on both sides, is not properly a contract at all; there is no promise binding either party to anything. To be a contract the transaction must be still *executory* or unperformed in whole or in part, that is, there must be a promise or promises binding one or both of the parties to do something. It follows that while a contract wholly executed no longer exists, it may be executed in part, and there will be frequent occasion to refer to this aspect of contracts.

4. *Essentials of a simple contract.*—The two essential elements of a simple contract are (a) mutual assent of the parties to the promise or promises constituting the contract, such mutual assent being expressed in some affirmative way capable of proof (unexpressed assent of a party provable only by his own testimony is not enough) and (b) a valid consideration or substantial reason for the promise or promises, also mutually agreed to by the parties in the same open way. A study in detail of these requirements and their application in a practical way to business transactions will make up the greater part of this chapter.

It is generally said that there must be also another requisite, viz., legal capacity of the parties to contract. But valid enforceable contracts may be made

by minors, lunatics and others who are classed as persons without capacity to contract. For instance, contracts of infants are valid until avoided by the infant, and always may be enforced by him against the other party. In all cases it is presumed that the parties are competent to contract until evidence establishes the contrary, and therefore it is better to say that in such cases the contract arises subject to the right of an incompetent party to avoid it in a proper case on proof of his incapacity. The incapacity of the parties as affecting the enforcement of the contract will be dealt with in detail hereafter.

Noted writers have asserted in the past that still another requisite must exist, viz., legality of the object or purpose of the contract, and legality of the consideration. But when the purpose or the consideration is illegal, actual contracts arise tho subject to the defense of illegality. As we shall see when the enforcement of contracts is discussed, many of these contracts are not void, and may often be enforced at least as to one of the parties. The better and now generally accepted view is that legality of the contract is not, therefore, a requisite to the making of a contract; illegality is rather a bar to its enforcement in a proper case.

5. *Mutual assent, how expressed.*—Assent to the promise must be openly and affirmatively expressed by both parties to the contract either by spoken or written words or by acts. The secret, undisclosed intent of either party is immaterial. This expres-

sion of assent usually takes the form of an offer by one party, the offeror, to the other, the offeree, and an acceptance of the offer. The offeror communicates to the offeree the terms of the promise by which he agrees to be bound in return for the consideration to be given or performed by the offeree, or he states the terms of the consideration which he will give for a promise which he desires the offeree to make. The offeree thereupon accepts the offer, either by speech or writing or by some open act of assent which may be legally proved. In this way the minds of the parties, as expressed by their words or conduct, have met in mutual agreement, and the contract, as expressed in the promise or promises involved, has arisen.

It is possible, of course, that a contract may arise without an offer and an acceptance, as when the two parties agree at the same moment to a proposed contract suggested by a third person, but in practice such a case is extremely rare, as one of the parties will usually assent even in such case before the other, in that way making the proposed contract his offer which is duly accepted by the other party when he gives his assent. These general principles must now be discussed in greater detail.

6. *Nature of offers and how made.*—An offer is a promise by the offeror to give or do something in return for a desired act or promise of the offeree. It is a conditional promise before acceptance, but when the offeree accepts, it becomes a contract, as the condition

is now performed, and the promise is based upon a valid consideration which is either the promise or act of the offeree. If the offer calls for a counter-promise from the offeree the acceptance results in a bilateral contract, a promise for a promise, one a consideration for the other, so that each promise becomes a good and binding contractual obligation. If the offer calls for an act, as where the owner of a dwelling promises to pay an agent a stated commission if he finds a purchaser of his house, no contract arises until the agent produces a purchaser ready, willing and able to buy the house on the terms stated by the vendor. The act of finding and producing a purchaser is what the vendor asks, not a promise from the agent to find such a purchaser, and that act is the condition attached to the vendor's promise to pay a commission, and therefore the only acceptance of the offer that was contemplated. As previously noted, these cases of offers accepted by acts of the offeree, not by counter-promises, are called unilateral contracts.

7. *Preliminary negotiations and advertisements.*—Negotiations inviting offers, or advertisements offering goods for sale at stated prices, are not offers, because they are not intended to be. The advertiser wants offers which he will be at liberty to accept or reject. It is obvious that a retail merchant advertising a special sale of merchandise in the press at special prices is not making an offer to any or all who might read the advertisement. Otherwise, ac-

ceptances might bind him to sell quantities of goods far beyond his power to deliver. In private negotiations the question may be a very nice one as to whether an offer is made to or invited from a correspondent. Thus a letter, "We are authorized to offer salt in car-load lots at 85 cents per barrel delivered at your city. . . . Shall be pleased to receive your order,"—answered by the telegraphic reply:—"You may ship me 2000 barrels Michigan fine salt as offered in your letter. Answer," was held not to be a contract principally because the letter put no limit upon the quantity, and therefore must have been intended as a bid for offers, not a promise conditioned upon acceptance. The quoting of prices on goods for sale by letter or telegram without limit as to quantity does not amount to an offer unless other circumstances make clear that an offer was intended.

8. *Preliminary agreement to be followed by a written contract.*—Frequently a parol, or spoken, agreement is made, in which all the terms of the contract are defined and agreed upon, with the understanding that it is to be finally put in the form of a written contract. If the parties agree either expressly or by clear implication that no contractual obligation shall arise until the written contract is signed, it is well-settled law that the preliminary agreement is mere negotiation leading up to the written contract which alone is to bind the parties. But in the great majority of cases the parties do not agree to anything of the kind. The mere fact that the con-

tract is to be put in written form does not make the parol contract inoperative. The minds of the parties having met in full mutual assent, and there being a valid consideration, a contract exists even tho a written contract is to be made, unless it appears affirmatively that the parties did not intend to be bound except by the written contract.

9. *Auction sales.*—The auctioneer in offering goods for sale to the highest bidder merely invites offers which he may accept or reject. Therefore, bids are offers which may be withdrawn at any time before the hammer falls; no contract arises until the goods are struck down to the highest bidder.

In the absence of a statute to the contrary, the auctioneer may withdraw goods from sale and he is not compelled to sell to the highest bidder, even tho the auction has been advertised as a sale “without reserve.” In several states, however, the statutes provide that, if the auction sale has been advertised to be without reserve, the auctioneer cannot withdraw the goods from sale. Massachusetts, Rhode Island, Connecticut, New York, New Jersey, Pennsylvania, Wisconsin, Michigan, Illinois and California are the more important states which have this statute.

10. *Advertisements for bids on public works.*—Like bids at auction sales, bids or estimates by contractors on public works submitted as a result of advertisements for bids are mere offers, and no contract arises until a bid is actually accepted. All bids, therefore, may be rejected even in cases where the

municipal authorities have no power to award the contract to anyone other than the lowest bidder because of a provision to that effect in the municipal charter.

11. *Offers must be communicated.*—Acceptance of an offer is, as we have seen, the manner and form of mutual assent. The offeree cannot accept that which he knows nothing about, and therefore, necessarily an offer must be communicated to the offeree before it can become a contract by acceptance.

12. *Rewards.*—The above principle is illustrated in cases of advertised rewards for the capture of a criminal, the return of lost property or other service. If the service is performed without knowledge of the reward, there is no contract since there was no offer communicated to the person who rendered the service, and consequently there could be no acceptance. In other words, there was no mutual assent. The weight of authority sustains this view, tho in several states the courts have held that the reward may be recovered, evidently because of the feeling that the advertiser should pay because he has received the benefit he sought.

If the services for which the reward is offered are rendered in part before the claimant learns of the reward and in part thereafter, he cannot recover, according to the authorities, because only part of the consideration is given in return for the promise. This does not affect the case of a man who has worked to accomplish the result sought thru the reward before knowing anything of it. Such work is

regarded as preparation; the actual accomplishment of the thing sought, such as the apprehension of a criminal, being the consideration for the reward, not work done toward that result. Thus a man may recover the reward if he actually makes the capture after learning of the offer, tho most of the actual work had been done before he became aware of it.

13. *Offers by mail.*—Offers made by mail, telegraph, etc., must be received before they are completed offers which may be turned into contracts by acceptance. The mailing of the letter or sending of the telegram is, of course, an overt act which is quite sufficient to prove the assent of the sender; but here as in all other cases of offers the offeree cannot give his assent by acceptance of the offer until he receives it.

14. *Indefinite offers and promises.*—An offer must be sufficiently definite so that the contract arising from its acceptance will be definite, expressing an exact meaning. An offer with alternative terms accepted as to one of the alternatives results in a valid contract.

If the offer leaves the time of performance indefinite, and it may reasonably be construed as meaning that performance is to begin or be completed within a reasonable time, an acceptance results in a valid contract calling for performance in accordance with that meaning. For instance, a contract to sell goods and fixing no time for delivery is construed as meaning delivery within a reasonable time. A

contract to do work of any kind with no statement of time for its completion calls for completion within a reasonable time.

On the other hand, a contract not to sue, not to engage in a stated business, not to use property in a forbidden way, etc., will be interpreted, when nothing is said as to time, as calling for perpetual performance; this, however, is true only of negative contracts of this kind.

Again an agreement to supply a commodity at a stated price for no specified time, or a similar contract to lease land, creates no obligation, as neither party is bound for any time, a reasonable time, obviously, not having been intended. This is also true of an agreement of hiring at stated wages by the day, week, month or year, when no period of service is fixed. If performance of the agreement is entered upon, a promise to pay for the goods delivered or the services rendered at the agreed rate will be enforced, but so far as the agreement continues to be executory or unperformed on both sides it is unenforceable since either party may refuse to go further with its performance. The fixing of wages by the day, month, or year does not fix the term of service, but only the rate of payment for the service actually rendered. A contract to work as long as the promisor is able, or so long as a business is carried on, is sufficiently definite, tho a promise for a "long engagement" would be unenforceable because of indefiniteness.

15. *Indefiniteness as to price, services or goods.*—When nothing is said in the offer as to price or wages it will be interpreted as meaning the reasonable value of the goods or services. But if the offer does not imply reasonable value, the agreement arising from its acceptance is void because too indefinite; for instance, pay “not exceeding \$300 per week,” a division of the profits “upon a very liberal basis,” “a part of the money.” In these cases the attempt to fix the price or basis of compensation excludes reasonable value as a basis but indicates nothing definite in its place.

When the work or property to be given is not expressed with any certainty the promise cannot be saved by the doctrine of reasonable value as in the case of indefiniteness as to price. A promise to erect buildings without a statement of dimensions or plans and specifications, to convey land “for services to be rendered,” to give employment, without stating what employment, are good illustrations of this rule.

In making or accepting an offer or in conducting a negotiation of any kind a business man should be careful to avoid indefiniteness as to all the terms of the proposed contract, stating clearly the time in which performance is to take place, describing with reasonable accuracy the goods to be delivered or services to be rendered, and the price or wages to be paid.

16. *Offers implied from acts or conduct.*—The usual offer is made definitely by speech or writing

duly communicated to the offeree. But an offer as well as an acceptance may be by acts or conduct of the offeror. The most usual case of this kind is a request for services made under such circumstances that the average person would expect that they would be paid for. An offer to pay their reasonable value will be inferred from the request for the services unless the facts of the case establish that the parties understood that they were to be gratuitous. Even if the services are rendered without any request for them, the performance of the services is a good offer resulting in a contract to pay their reasonable value if they are accepted by the offeree with knowledge that payment for them is expected.

The question in these cases is one of fact as to whether the parties as average persons intended that the services should be gratuitous or not. They will be gratuitous in cases, for instance, of minor services between members of the same family, when two physicians or lawyers have been regularly in the past giving professional services to each other without compensation, when a neighbor as a merely friendly act introduces a purchaser of real property without any expressed intent of asking for a commission. In the absence of circumstances of this nature, however, the request for the service, or the acceptance of it, gives rise to a contract to pay its reasonable value.

17. *How offers are terminated before acceptance.*—When the offer specifies a time within which it must be accepted, it remains good during that time

only, and an acceptance thereafter is void. When the offer fixes no time for acceptance the law provides that acceptance must take place within a reasonable time. When the offer is made in conversation with the offeree, he must accept during the conversation, unless he is given further time expressly or impliedly. If the parties are at a distance from each other the question of what will be a reasonable time within which acceptance must be made will depend on the circumstances of the case.

An offer to buy or sell a commodity subject to rapid fluctuations in value must be accepted very promptly, especially if the offer is made by telegraph. Thus an offer by telegraph to sell oil and answered by a telegram sent twenty-four hours later, was held not to have been accepted in time. A longer time is deemed to be reasonable in answering offers to sell real property. Five days has been held to be a reasonable time, while two weeks has been held to be too long a time in these cases.

Offers by letter or messenger accepted by answers sent the same day will be accepted in time in all cases, even when an answer by return mail is specified. When nothing is said in the offer about time of acceptance in these cases a longer time will generally be allowed as reasonable, except in those commercial transactions in which the customs of business require a prompt acceptance.

Offers calling for acts resulting in unilateral contracts necessarily remain open during the time rea-

sonably needed to complete the act. Thus a reward for the conviction of a criminal remains open until conviction is barred by the Statute of Limitations.

18. *Termination of offers by rejection.*—The rejection of an offer by the offeree ends the offer so that it cannot be accepted thereafter. A counter-offer, modifying the terms of the original offer, operates as a rejection, so that an acceptance of the original offer sent thereafter is void. Care should be taken by a man who desires to negotiate for better terms, but who intends to accept the offer if better terms cannot be had, not to make his communication in the form of a counter-offer. He should simply ask whether or not the offeror would be willing to modify his offer in the way desired. In case of a refusal to do so, or of a failure to get a reply, he could then accept the original offer, provided it had not lapsed by the passage of time. Thus where an offer for iron at 40 shillings was answered, "Please wire whether you would accept forty for delivery over two months," and the offeror thereupon sold the iron elsewhere and sent notice thereof to the offeree, it was held that an unconditional acceptance dispatched by the offeree before receiving the notice of sale resulted in a contract.

19. *Rejection by mail or telegraph.*—A rejection by mail or telegraph, whether in the form of an express rejection or of a counter-offer, puts an end to the transaction when the rejection reaches the offeror. It will be noted later that when the offer

contemplates or permits a reply by either method, the mailing or dispatching of the answer is an overt act expressing the intent of the offeree in the way contemplated by the offeror and readily capable of proof; therefore, as an acceptance it binds the offeree. This is settled law in most states as to acceptances by mail, but there is very little authority as to whether the same rule applies to the corresponding case of rejections.

20. *Revocation of offers.*—Every offer may be revoked before acceptance. The offeror does not intend to be bound by any promise arising out of his offer until it has been duly accepted. An express promise to leave the offer open for a stated period does not prevent the revocation, as it does not bind the offeror as a promise because of lack of consideration.

The revocation of an offer must be communicated for the same reason that requires the communication of the offer. Just as the *communicated intent to be bound* is necessary before a contract can arise by acceptance, so the *communicated intent not to be bound* is necessary in the case of revocation to prevent the contract which otherwise would arise by an acceptance. That is why the mailing of a letter or the sending of a telegram revoking an offer has no relation to the cases of acceptances or rejections by letter or telegram discussed in the preceding section. Mutual assent makes necessary the communication of the offer. Communication of the revocation is

just as necessary to prevent that mutual assent which would otherwise certainly arise as a matter of law resulting in a contract if the communicated offer is left for acceptance with the offeree.

A sale to someone else, of the property offered or any other act necessarily inconsistent with a continuation of the offer, will amount to a revocation if the offeree learns of it before acceptance. In spite of arguments that he should not be compelled to rely on hearsay statements of third persons, and that since the offer must come from the offeror so must also the revocation, the prevailing rule is that he cannot accept if he has notice that the property has been otherwise disposed of. He can easily verify the correctness of his information, and the impropriety of allowing him to accept the offer of the property when he knows it has been otherwise disposed of is too clear to require discussion.

21. *Revocation of offers by advertisement.*—Offers of rewards, and the like, by advertisement in the press may be revoked by publication of a revocation in the same way and to the same extent substantially as the original offer was published.

22. *Revocation of offers to pay for acts.*—When the offer calls for an act, as to move a safe from one building to another, to find a purchaser for real property, and the like, it can be accepted, as we have seen, only by performance of the act. The promise of the offeree is not asked for nor given, nor does he assume any obligation to complete the act by starting the

performance of it. Theoretically, there can be no doubt that the offeror may revoke his offer at any time before the act is completed, tho the hardship and injustice of this to the offeree has led to much speculation among legal writers as to how it may be avoided. There is no doubt that where the offeror has received benefits he will have to pay the reasonable value of the work done up to the time of revocation on the theory of a quasi-contractual obligation¹ implied by law to prevent unjust enrichment of the offeror. There seems to be no good reason why the same doctrine should not extend to all cases of detriment suffered by the offeree due to the unjust refusal of the offeror to let him complete the act tho the offeror has received no benefit. The case of a real estate agent employed to sell real property for a commission does not come under any such rule, as by custom in that business he takes the chance of a sale of the property by other brokers or its sale or withdrawal by the owners before the broker finds a purchaser, so that he is entitled to nothing unless he finds a purchaser before the property is withdrawn. The law is exceedingly indefinite on the principal question. By weight of authority the offeror may revoke, subject to liability in quasi-contract for the reasonable value of all benefits received by him thru part performance.

23. *Termination of offers by death or insanity.*—

¹ For a definition and explanation of quasi-contract see Chapter XXIV, hereafter.

Death of either party before acceptance terminates an offer. Notice of the death of one party to the other is not necessary.

The effect of insanity upon contracts made by the insane person is, under the modern cases, a complicated matter involving much more than the principles of offer and acceptance, and will be discussed in a later chapter dealing with capacity of the parties to a contract.

24. *When offers are irrevocable.*—An offer to sell, made to be accepted within a stated time, for which a consideration is paid, is a contract to sell on the terms stated and is binding on the offeror because of the consideration received from the offeree, on condition that the offeree accept the offer. The offeree is bound to nothing before acceptance; he may accept or not as he pleases. More frequently this contract, called an option, is in the form of an offer accompanied by a collateral promise to leave the offer open for a stated time in return for a consideration. There is no difference, other than that of mere form, between these transactions, and exactly the same law applies to each. In each case the seller or vendor contracts to give the buyer or vendee a contract of sale at the vendee's election within the time specified. If he revokes the offer in either case he breaks the contract of option, and in either case the damages which he must pay will be the same, viz., the value of the contract of sale to which the offeree had an optional right. The amount of damages will be exactly

the same as if the contract of sale had been formally entered into by exercise of the option, and had then been broken.

If the subject-matter of the sale is land, the offeree is entitled to the land rather than to damages, and therefore, the contract will be specifically enforced. But if the subject matter of the sale is personal property, all the offeree may recover is damages, exactly what he would have recovered if the option had been exercised and the vendor had thereafter been guilty of a breach of his contract.

REVIEW

State into what three general parts the law of contracts is divided.

Explain the two general types of contract.

Name the essentials of a simple contract.

Explain what constitutes an offer, and distinguish it from an invitation to make an offer.

State the rules of law as to the revocation of an offer.

CHAPTER III

CONTRACTS—THE ACCEPTANCE

1. *Acceptance of offers.*—As explained in discussing offers, acceptance of an offer is essential to mutual assent of both parties to the contract. Neither intends to be bound except as both are mutually bound, and, therefore, the offer must be communicated to the offeree and accepted by him in order that a contract may arise. This would be equally true tho a consideration of value were not necessary.

Acceptance of an offer which calls for a promise from the offeree requires either that the acceptance be communicated or be put in the way of communication, as the offer from a distance, either by letter, messenger or telegram, clearly calls for an answer by the same means of communication or by one equally quick and safe. It is settled by the great weight of authority that the mailing of a letter or the sending of a telegram is a complete acceptance where the offer may be accepted in that way, and the contract arises at that moment, not when the letter is received, so that a valid contract exists even when the letter or telegram is lost, or when the offeror dies before its receipt. Thus also a rejection of the offer, made personally to the offeror after the letter of ac-

ceptance had been mailed but before its receipt, would be too late, the contract having arisen on mailing of the acceptance.

2. *The acceptance must not modify the offer.*—If, as before stated, the offeree modifies or changes in any material way the terms of the offer it amounts to a rejection. Such an attempted acceptance is regarded as a counter-offer, and must be accepted by the original offeror in order that a contract may arise. To operate as a counter-offer it must reach the original offeror, tho as a rejection it will be complete when mailed if an answer by mail was called for by the original offer. The adding of any new terms or conditions or the changing in any material way of any of those appearing in the offer will have this result. For illustration, an acceptance providing that any of the terms of the contract are to be settled later; an attempted acceptance changing the place of payment, modifying the method of payment or of performance of the contract in any other respect, or containing new provisions as to the quality of the goods, time or place of delivery, etc., are counter-offers and, therefore, insofar as the original offers are concerned, amount to rejections instead of acceptances.

The specification, in the acceptance, of terms not expressed in the offer but implied by law is not a modification of the offer, and a valid contract results. An offer to sell land accepted with the proviso that the title shall be good illustrates this. In any case an unqualified acceptance is not affected by a re-

quest for a modification of the offer, provided it is stated clearly that the offer is accepted whether the requested modification is made or not.

3. *Acceptances by mail, telegraph or telephone.*—The offer must expressly or impliedly authorize reply by mail, telegraph or telephone to make the mailing of a letter or the dispatching of a telegram a valid acceptance. This is implied in all cases in which the offer is made in the way in which the reply is sent; also where an offer by parol in which time is given to answer is followed by a distant separation of the parties, a reply by mail is impliedly authorized; a reply by telegraph will also be good in a case of that kind if in accord with the customs of business men in similar transactions. Of course, the letter of acceptance must be properly stamped and addressed, so that it will go forward in the usual way, and therefore the lack of an extra stamp for a letter of unusual weight will not prevent the contract from arising when the letter is mailed, as its delivery is not impeded by that circumstance. Depositing a letter in a public mail box, or delivering it to a postman on his rounds, is a complete mailing. Giving it to anyone else to mail is not enough to create a contract.

A contract by telephone involves a conversation at a distance, and acceptance must be made during the conversation unless a longer time is given, exactly as in the case of offers in person. The contract arises, however, at the place where the offeree speaks

the words of acceptance, not at the place where the offeror hears them.

In all of these cases the offeror may provide in his offer that acceptance must be received before a contract shall arise. By doing this a business man may protect himself from the uncertainties and dangers of loss that may arise thru delayed or lost letters and telegrams in reply to his offers.

4. *Effect of actual receipt of acceptance before offer lapses.*—An offer calling for an answer by return mail is accepted by any actual communication to the offeror within the time a mailed acceptance would be received. If an answer is not sent by return mail, but after waiting too long for a reply by mail the offeree sends an acceptance by telegraph which is actually received as soon as a letter by return mail would have been, a good contract arises. In the same way, tho a mailed acceptance fails because of a defect in the address, a telegraphic or telephonic acceptance will be good, provided it is actually received within the time intended by the offeror.

5. *Acceptance of offer calling for an act, not a promise.*—As explained heretofore, an offer calling for an act can be accepted only by performance of the act. No contract arises until the act called for by the offer has been completed. Notice of its performance need not be given. The contract arises by performance of the act, an overt act of acceptance which automatically turns the offer into a contract,

since it constitutes the condition as well as the acceptance necessary to mutual assent.

There are some cases, however, where as a reasonable matter it is clear that the offeror intended that notice should be given him of the act of acceptance on the part of the offeree. The most important of these are contracts of guaranty. An offer to guarantee payment, if credit is given to the person whose credit is guaranteed, reasonably involves the requirement that when the credit is given, the creditor notify the guarantor within a reasonable time so that he may know of the extent and character of his obligation thus arising; this is something about which he could not readily get information otherwise. The contract of guaranty arises when the act called for, viz., the giving of credit to the third person involved, is performed. It is then too late for the guarantor to withdraw his offer. But the contract is subject to a condition that notice be given him and he is relieved from liability if such notice is not given within a reasonable time.

6. *Acceptance implied in fact.*—Just as an offer may be inferred from conduct without speech or writing, so an acceptance may be made in the same way. Accepting goods offered for sale at a stated price is an acceptance of the offer and implies a promise to pay the price. Acceptance of services implies a promise to pay at the rate expressed in the offer or their reasonable value if no amount or rate is so expressed.

7. *Effect of acceptance of writings.*—A writing accepted by a person as his contract, whether signed by him or not, binds him to what it expresses. A bill of lading or express receipt accepted by a shipper of goods binds him to the terms of shipment contained in the writing. The printed terms appearing on a telegraph blank of the company binds the sender of a dispatch written by him on the form. In some states this has been qualified so as to require proof that the conditions on the receipt or other instrument have been brought to the attention of the shipper where the type in which they are printed is very fine, or they appear only on the back of the instrument. Acceptance of a deed conveying land binds the grantee to any covenants contained therein, such as an agreement to assume payment of a mortgage on the property, tho he has not signed the deed.

8. *Signing or acceptance of writings by illiterate persons.*—Any person, whether illiterate or not, is presumably liable on any contract signed by him, whether he has read it or not, and whether or not he is ignorant of its contents. The principle runs all thru the law of mutual assent in contract that the actual meeting of the minds is not necessary; it is the mutual assent as expressed by their acts which is involved, and a person is charged with the ordinary meaning and consequences of his acts, including the execution of written contracts.

If an illiterate person is misled by false statements as to the contents of the instrument, or any person

whether illiterate or not is fraudulently induced by the other party to it to sign a document without reading it or having it read to him, the contract, will, of course, be set aside because of the fraud. The need of examining carefully every written instrument before signing or accepting it in any transaction is, therefore, obvious to every business man.

9. *Acceptance by silence.*—Silence alone rarely amounts to acceptance. The keeping for an unreasonable time, of property sent on approval, or any acceptance and use of property offered for sale, are acts of acceptance in and of themselves which give rise to a contract, not the silence of the purchaser. The case of periodicals sent to a subscriber after his subscription has expired, or to one who has not subscribed for them, presents much the same situation. The keeping and use of the periodical gives rise to the inference of acceptance rather than the silence of the offeree. So too, regarding contracts of service discussed under offers, the acceptance of the services with knowledge that payment is expected is what creates the contract, not the silence.

10. *Mistake of the parties as to terms of the contract.*—A mistake by either or both parties as to the terms of a contract and its meaning does not prevent a contract from arising. It may be a reason for a modification in its enforcement on equitable grounds, but the contract arising from the words or acts of the parties is not what they may have actually intended, but what an average person would say they intended,

interpreting their words and conduct as their expression of intent. It is for this reason that a mistake made by a person used to communicate the offer and acceptance will bind the person making use of that person as an intermediary. For instance, when the offeror asks a telephone operator to repeat his offer to the offeree, or when an offer or acceptance by telegraph is not sent in the correct form, it will bind the sender in the form in which it was received.

REVIEW

Explain what constitutes an acceptance of an offer and distinguish it from a counter-offer.

State the principles of law which determine when an acceptance occurs and the contract is completed.

Discuss cases in which contracts are inferred from the actions of the parties rather than their words.

Explain the effects upon the contract of mistakes as to the subject matter and as to matters of law.

CHAPTER IV

CONTRACTS—CONSIDERATION

1. *General nature of consideration.*—A promise not under seal is not valid unless a sufficient consideration is given for it. This doctrine exists only in the United States, in England and in the British Dominions in which the English system of law prevails. It is a highly technical doctrine, which arose historically in a haphazard, almost accidental, way. The fundamental nature of consideration will be explained in discussing the practical rules of the law in applying the doctrine.

2. *Consideration, a benefit to the promisor or detriment to the promisee.*—The fundamental basis of the law of consideration is that the law will not enforce a promise which is simply a gratuity or gift. The promisee must give or do something at the request of the promisor which is either a benefit to the promisor or a detriment in the legal sense to the promisee. It may not be a detriment in the ordinary sense of the word, as where the promise is to pay a sum of money to the promisee if he will refrain from drinking intoxicating liquors, or from any other harmful practice. The giving up of such practices will be, ordinarily speaking, a benefit rather than a detriment to

the promisee, yet it is a detriment to the promisee in the legal sense, since he has refrained from the practice tho not obliged to do so. Such promises are valid contracts when the consideration asked for has been given even tho resulting in no benefit to the promisor; the promisor gets what he asks for. Adequacy of the consideration is immaterial provided it is what the parties intended.

3. *Consideration in unilateral contracts.*—In nearly all cases where the offer calls for an act rather than a counter-promise, resulting in an unilateral contract, the act will be a detriment to the promisee even tho it will also be a benefit to the promisor, and this has resulted in the argument that detriment to the promisee may be taken as the test in all cases, since it will be immaterial whether a benefit to the promisor exists or not. This is true in the usual business contract, which calls for some act or thing from the promisee which the promisor wants, whether it will be a benefit to him actually or not. All that the law insists on is that the promise be something more than mere gratuity, and certainly the receiving of a benefit by the promisor which he has requested proves that the promise was no gratuity. It is therefore better to adhere to the generally accepted form of the rule that a valid consideration must be either a benefit to the promisor or a detriment to the promisee. We shall see that in one class of cases a benefit received by the promisor is not a consideration, according to the weight of authority, viz., where the act requested

by and performed to the benefit of the promisor is an act which he is already bound to perform by a valid contract with some third person. Is the promise given for such an act a mere gratuity when the promisor has received the benefit he expected? Is there any reason why the promise should not be enforced as the parties intended? These questions must be answered in disposing of this class of cases.

4. *Consideration in bilateral contracts.*—In the usual business contract in which mutual promises are made there is no real difficulty in finding the technical consideration which the law requires. Each promise is given in consideration of the other. They take effect as legal promises at the same moment, and each party gets for his promise exactly what he wanted, viz., the promise of the other party which is, in the usual case, valid and enforceable. But difficulties arise in certain cases which will be separately considered in the following section.

5. *A promise to do something which the promisor is already bound to do is not a valid consideration.*—A promise to pay a debt is not a valid consideration for another promise. The debtor adds no new detriment by his promise, nor does the creditor get any new benefit. The one was already bound to pay and the other entitled to receive the money due. Payment of part of the debt is, therefore, not a valid consideration for an agreement that the entire debt be discharged; payment or promise to pay a debt in whole or in part is not a good consideration for any

other promise made by the creditor, as to give a power of attorney to discharge a lien, to release a claim of any kind, and the like.

A promise not to sue upon a groundless claim, or to give up such claim is not a valid consideration. No man has a legal right to try to enforce a claim which is admittedly without foundation legally, and, therefore, foregoing such claim, or promising to do so, is neither detriment to the claimant nor benefit to the person receiving such forbearance.

A promise to perform an act which the promisor is already bound to perform by contract with a third person is not a good consideration, since performance of the act would not be. The promisor is already bound, and, therefore, he suffers no detriment in performing the act or in promising to perform it. This is the prevailing view, tho some courts hold that the promisor may bind himself to another to carry out an existing contract.

In all these cases it is clear that the promise itself is not a good consideration unless the performance of it would be. For the same reason a promise which cannot be enforced because of indefiniteness, as explained in the preceding chapter, will not be valid as a consideration for another promise. The same test of the consideration required to make a promise enforceable applies to both unilateral and bilateral contracts: if actual performance is sufficient then a promise to perform will be, but if such performance will not be valid as consideration, a promise to per-

form will not. In either case, there must be benefit to the promisor or detriment to the promisee.

6. *Contingent promises are valid as consideration for counter-promises.*—A promise contingent upon the happening of some event may never be actually enforceable as the condition may never happen, yet the promise is of value as consideration and will make the promise for which it was given valid and binding. As explained above, indefinite promises, such as to buy such goods as the buyer “may want,” are void because they are not legal promises and bind the promisor to nothing. But a promise to buy as much as the buyer may need in his business, amounting to an agreement not to buy elsewhere, is a good consideration, tho it may be that because of discontinuing his business the buyer may not need any goods. It, however, is a good conditional promise. For the same reason, a promise to employ a man “for a period of time during which the corporate business might be carried on” is a valid consideration for the employe’s promise to serve. In these cases the benefit and the detriment exist in fact. The promise is not a gratuity but a valid business transaction which the law will enforce.

7. *Contracts under seal.*—A promise executed as a sealed instrument is valid as a gift. The special form and ceremony with which the transaction was invested under the ancient law made the promise binding. This is still the law except in some states where by statute, as in New York, it is provided that the

seal creates a presumption of consideration, but if it is proved as a defense that no consideration was in fact given for the promise, the promise will be unenforceable.

Contracts in writing not under seal require a consideration exactly as when made by parol. Consideration as an element in negotiable instruments is discussed in the chapter on that subject.

8. *Gratuitous conditional offer distinguished from offer calling for an act as consideration.*—If one should say to a beggar; "If you come around to my house I will give you a meal," no contract would arise when the beggar performed the condition by coming to the house. The act was requested not as a consideration of value to the promisor, but in order that the promised gift might be made. Close cases involving this distinction have often arisen. Thus where a reward of £100 was offered to anyone who contracted influenza after using a smoke ball manufactured by the defendant, it was held that the purchase and use of the ball was a good consideration for the promise. A promise to pay his nephew's expenses on a trip to Europe was held to be binding on the promisor, the taking of the trip being the consideration.

On the other hand take this case. In a letter to his widowed sister the defendant said, "If you will come down and see me, I will let you have a place to raise your family . . . on account of your situation and that of your family I feel like I want you and

your children to do well." This was followed by his sister's moving with her family and occupying a house supplied by the defendant for two years, after which she was requested to move. The promise was held to be a gratuitous conditional promise, the moving to his place by his sister not being asked for as a consideration.

These cases turn on a question of fact, as to whether or not the offer should be reasonably construed as offering a gift or an enforceable promise in return for an act asked for by the offeror. A helpful test is to inquire whether the act requested was in any way a benefit to the promisor. If so, it will be generally interpreted as a valid consideration. In cases of doubt, where either interpretation may be taken, the suffering of the detriment by the promisee will usually be held to be a consideration rather than a mere condition of a gratuitous promise.

9. *Consideration may be a benefit to a stranger.*—If the promisee incurs a detriment at the promisor's request which is a benefit solely to a third person, it has been settled law from almost the beginning of the law of simple contracts that a valid contract arises; the detriment asked for by the promisor has been incurred. Contracts of guaranty in which credit is given to the debtor, a third person, by the creditor at the request of the guarantor or surety is the most usual situation of this kind. The question of whether the consideration must be given by the promisee or may be given by a third person will be discussed in

the sections dealing with contracts made for the benefit of third persons.

10. *When payment of or giving of security for a debt is a valid consideration.*—While, as above noted, a promise to pay a debt is *not* legal consideration, payment of the debt before it is due, or at a different place, or the giving of security, or any other act which the debtor is not bound to do, *is* a valid consideration for a promise to release part of the debt, or other promise on the part of the creditor. Payment of the debt by giving a note made by a third party for a smaller amount, or by a note of the debtor for a smaller amount indorsed by a third person, is a good consideration for the creditor's agreement to accept it in full payment. But the debtor's note or check unindorsed by another person is not a valid consideration when for a sum less than the amount of the debt. It is a payment or promise to pay part of the debt which the debtor is already bound to pay. Payment of a debt by note or check for the full amount of the debt is good, if both parties so understood the transaction. When nothing is said about it the general rule is that payment is conditional upon the note or check being paid when due; if dishonored the original debt is restored.

11. *Extension of time to pay a debt.*—An agreement by debtor and creditor to extend the time to pay a debt is valid, provided it is subject to the payment of interest, the promise of the debtor to let the debt stand subject to interest for the extended time being

a good consideration for the creditor's promise to extend the time of payment. It will be void if the debt does not carry interest, as in that case the debtor incurs no detriment nor does the creditor receive a benefit for the creditor's promise.

12. *Payment in full settlement of claims uncertain as to amount or disputed.*—Any amount accepted in full settlement of a claim for damages in which the amount is not fixed or certain, is a good consideration. Each party gives up his right to demand a judgment in court more favorable to himself. The same is true of any claim for a fixed sum, when the claim is honestly disputed, the surrender of such a claim is a valid consideration for a promise to pay a sum agreed upon by way of compromise. But if the claim is a debt for a fixed sum and is not and cannot be honestly disputed, any compromise agreement for a smaller sum, or payment of a smaller sum, is void. There is no detriment to the debtor or obligee, and no benefit to the creditor. It is a mere gratuitous promise to give up part of the debt.

13. *Special inducements to fulfil existing contracts.*—The performance or promise to perform an existing contract is not a valid consideration for a promise to pay the contractor more money. Cases of this kind arise when a contractor refuses to perform his contract unless the other party to the contract agrees to pay him a larger amount. The contractor cannot enforce such a promise because

he has given nothing for it; it is gratuitous as the contractor was already bound to perform his contract.

14. *Promise to perform existing contract with third person.*—There has been great diversity among legal writers on the question as to whether or not a promise to perform an existing contract with a third party is good consideration. The great weight of authority in the United States sustains the view that a second promise given to another person to perform an existing contract theretofore made with a third person is not a good consideration, and performance of the original contract will not be a good consideration for a promise to pay the contractor for doing that which he was already bound to do. In England, and also in Massachusetts, Illinois and New Jersey, however, the courts hold that the second contract is valid, provided the performance of the original contract with the third party will be of benefit to this second promisor who undertakes to give additional compensation to the contractor for performing his original contract. There can be no doubt that the contractor suffers no detriment in return for the new promise, as he is already bound to carry out his original contract, but if the actual performance of that contract will be a benefit to another it is difficult to see why a promise to pay for such performance should be treated as a promise to make a gift which the law will not enforce. If performance of the

original contract benefits this second promisor he should be allowed to secure this benefit by promising to pay for it, a reasonable business transaction which the law should enforce.

15. *Doing or promising to do what the party is bound by law to do is not consideration.*—A promise to pay a policeman, fireman, district attorney, sheriff or other public officer for merely doing what he is bound to do as such officer is not a valid consideration, as the officer incurs no detriment nor does the promisor get any benefit to which he was not legally entitled. Of course, if the officer is promised a reward for doing something beyond and outside of the scope of his public duty, the performance of such an act will be a valid consideration for the promise of reward.

16. *Past consideration.*—A promise to pay for an act completed before the promise was made is not good because there is no consideration for it. It is a mere gratuity, since the completed act is not done in consideration of the promise because it was completed before the promise was made. Cases of ratification of an infant's promise after he becomes of age, of ratification by a principal of an unauthorized act of his agent, of promises to pay debts or claims barred by the Statute of Limitations, are all special cases based on entirely different principles and not identified with this question. They will be treated in detail later.

REVIEW

Explain what constitutes good consideration in both unilateral and bilateral contracts.

Discuss the validity of consideration when a man promises to do something which he is already bound to do.

Distinguish between a gratuitous conditional offer and one calling for an act as consideration.

Discuss extension of time to pay a debt from the standpoint of valid consideration.

Define the status of a promise to pay a policeman or other public officer for doing his duty.

CHAPTER V

CONTRACTS—PARTIES AND FORM

1. *Validity of contracts.*—Generally speaking, the courts will uphold the agreements into which individuals enter. It is the purpose of the law to carry out the intent of the parties. All that is required is that this intention of the parties should be clearly evidenced by their words or acts.

This general rule is, however, subject to some exceptions. There are classes of persons who in law are wholly or partially incapacitated from making contracts. Again certain contracts are of such a nature that it has been found desirable to stipulate the nature of the proof required if they are to be enforceable at law, in other words, to prescribe the form of the contracts. With these two aspects of contract law, the present chapter will be concerned.

2. *Infant's contracts.*—Any person under twenty-one years of age is an infant in the eyes of the law. A contract made by an infant is good and may always be enforced against the other party; but it cannot be enforced against the infant if he chooses to avoid it by setting up his infancy as defense. However, if he ratifies it after becoming twenty-one, it is then binding on both sides.

In many states a woman becomes of age at eighteen by statutory provision, and in a few states marriage of an infant gives him or her full power to contract.

Conveyances of land and sales of personal property and other transactions executed by an infant are governed by the same rules. They are good until avoided by the infant, and they are made valid in every respect when ratified by the infant after he attains full age. Conveyances of real property cannot be disaffirmed until the infant becomes of full age, but sales of personal property and other transactions may be avoided by the infant during his minority.

In these cases of executed transactions in which the infant has received the benefits of performance by the other party, the more usual rule is that the consideration need not be returned by him as a condition of avoiding the contract, tho of course the other party will have the right of action to recover his property after the infant has disaffirmed the contract. In New York and several other states, however, it is held that as a condition of disaffirming a contract the infant must return what he has received under it.

3. *Contracts for necessities.*—Contracts for necessities, like other contracts made by infants, are binding on the other party. But if the infant elects to disaffirm, he must pay the reasonable value of the goods or services received by him if they are “necessaries” in the legal sense. Since he is not held for the contract price, but only for the reasonable value

of the goods or services actually received by him, it is clear that he is held, not on his own promise, but on a promise implied by law to pay their reasonable value.

Necessaries in the legal sense will vary with the wealth and station in life of the infant. Essential articles of food and clothing and essential services of doctors, dentists and nurses are necessities if reasonably necessary to the maintenance of the infant. It must be remembered, however, that contracts for such things or services will not bind him if he is already supplied with what he needs or with money sufficient to supply his wants.

A merchant supplying an infant with merchandise cannot recover in an action against the infant unless he is able to prove that his father or guardian has failed to supply him with what he needs for his reasonable maintenance, and where he lives at home the presumption is strong that he is receiving all that he requires according to his station in life. If he is living away from home, the merchant must prove, not only that the things supplied are what are generally understood to be necessities, but also that the infant was actually in need of them and had no money to pay for them at the time of the purchase.

A parent in duty bound by law to support his child will be liable to others for necessities supplied the infant only where the parent has failed in his duty to supply him with such necessities or the money with which to buy them, or where a special emergency

exists calling for immediate action, and then only when the purchase was made on the parent's credit. Of course, if the parent consents to the purchase on his credit he will be bound, whether the goods or services supplied are necessities or not.

4. *Insane persons as parties to contracts.*—A contract made by an insane person may be avoided by him, but it is binding upon the other party unless avoided by the lunatic or, on his behalf, by his guardian or committee. This is true whether the other party knew of the lunacy or not. The old cases holding that a lunatic's contract is absolutely void have been overruled. It is, therefore, always binding on the other party, the election between disaffirming and ratifying being entirely for the lunatic or those acting for him.

The modern cases have gone very much further even than making the contract voidable. They hold that if the other party to the contract had no knowledge or notice of the insanity the contract cannot be avoided by either party, if the contract is fair to the lunatic, in that no advantage is taken of him. There is no doubt about this in cases where the contract has been partly performed so that the other party cannot be restored to his former position. Tho there is some authority supporting the position that a purely executory contract, nothing having been done toward its performance on either side, cannot be avoided by the lunatic where the other party had no notice of the lunacy, the weight of authority

is the other way, and the contract may be avoided by the lunatic or on his behalf. When the contract has been partly executed by the other party the weight of authority favors the rule that the lunatic may rescind provided the consideration received by him is returned.

5. *Acts of adjudged lunatic void.*—After a man has been adjudged a lunatic in lunacy proceedings and a committee or guardian has been appointed to act for him, all acts of his are absolutely void, because his committee or guardian alone can transact his affairs. As stated above, his committee or guardian may disaffirm or ratify voidable contracts and transfers of property made by the lunatic before their appointment. Contracts or conveyances made by him after their appointment are void for all purposes.

6. *Drunkenness.*—Incapacity from drunkenness exists legally when it renders a person incapable of understanding the contract or other transaction involved. A lesser degree of intoxication does not amount to legal incapacity. If legal incapacity exists from this cause it renders the contract, conveyance or other transaction voidable at the intoxicated person's election. In practically all cases in which the parties deal with each other in person the other party will have notice of the condition. The situation was well expressed by a New Jersey court which stated that the drunkard will be liable to the other party unless his condition was "brought about by the other party, or unless it was so total as to be palpable

evidence of fraud in the person entering into a contract with one so intoxicated.”

7. *Married women*.—The disabilities of the common law upon a married woman's power to contract and to own, convey and devise property have been removed completely or nearly so in most of the states. In the majority of the states she may contract as freely as tho unmarried. In many states she cannot enter into a contract of suretyship; in some she cannot contract with her husband; in others she cannot contract to give her personal services without her husband's consent. Again in several states she cannot convey land unless her husband joins with her in the conveyance. The details of these varying laws can be ascertained by consulting the statutes of the different states.

8. *Contracts made for the benefit of third persons*.—Promises made by one person to another which are for the benefit of a third person and are intended to be enforceable by him arise in two classes of cases: (a) when no benefit is derived by the person securing the promise, the sole benefit from its performance being received by the third person; and (b) when the promise calls for the payment or discharge in whole or in part of a debt or other obligation from the person securing the promise to the third person, performance, therefore, being for the benefit of both.

In England, Massachusetts and a few other jurisdictions, by clinging literally to the technical forms of the usual simple contract with only two parties, the

courts have refused a remedy to the third person, contrary to the intent of the two immediate parties to the contract and resulting in a very clear case of failure of justice.

In New York and the great majority of the States of the Union, however, it is settled law that the third party as beneficiary may sue in all these cases if it appears that the immediate promisor and promisee intended that he was to have the right to enforce the promise (i. e., if the promise were really for his benefit in that sense) and that the person securing the promise did so as part of a valid business transaction which ought to be enforced and not as a mere gratuity to the beneficiary.

9. *Third person as sole beneficiary.*—The first class of cases, in which the beneficiary alone gets a benefit from performance, is illustrated by life insurance policies. The beneficiary may now sue on the policy everywhere in the United States, statutes so providing in the few jurisdictions where technical decisions of the courts had held otherwise. It is obvious that such a contract is a valid business transaction, something very different from a mere executory gratuity which the law refuses to enforce. It is obvious in all cases of this kind that the beneficiary alone was intended to be benefited and that he alone could show damages for a breach. Therefore, he alone was intended to have the right to enforce it.

10. *Promisee and third person benefited.*—In the second class of cases the promise calls for the payment

or performance of a debt or obligation owing from the promisee who secures the promise to the third person who in turn gets the immediate benefit of performance. In such situations there has been almost endless discussion by law writers and judges, resulting in many conflicting theories, which are exceedingly confusing to a trained lawyer, and of no value whatever to a business man. It is enough for our purpose to know that in nearly every state of the country it is now settled law that such promises may be enforced by the third person as beneficiary provided it appears (a) that some debt or obligation exists from the person securing the promise to such third person, and (b) that the parties intended the promise for the benefit of the third person in the sense that he was to have the right to enforce it.

11. *Assumption of mortgage debt.*—One of the commonest cases illustrating these contracts is the promise to assume or pay a mortgage indebtedness by a man who buys real property subject to a mortgage. Because of the mortgage, he pays less by the amount of it and if he promises to pay the mortgage indebtedness to the mortgagee in consideration of the conveyance of the land to him it is clear that he and the vendor both intend that the mortgagee shall look to him as the primary debtor, and that the mortgagee shall have the right to enforce the promise of assumption made by the purchaser of the land. The securing of such a promise by the vendor of the land as part of the transaction is not a mere gratuity

to the mortgagee; it is part of a valid business transaction which the law is bound to recognize and enforce.

If, however, the person securing the promise in any of these cases owes no debt or obligation of any kind to the third person, then he has no business securing such a promise; he is a mere officious intermeddler with a matter that does not concern him, and the promise which he secures for the benefit of a third person is a mere gratuity which the law will not enforce. Therefore, if a man who buys property subject to a mortgage without assuming the mortgage debt thereafter conveys the property to another who assumes the debt, the promise to assume the debt cannot be enforced by the mortgagee, since this man who secured it, not having assumed the debt, did not owe it. He had no business securing such promise from his purchaser of the land. It was a gratuity, in no way for his benefit, and therefore not a promise which the law will recognize and enforce.

12. *When contracts must be in writing.*—Contracts under seal, called specialties, must be in writing in order that the necessary seal may be attached. The seal, not the writing, is the distinctive requisite of these contracts which gives them their peculiar effect. All other contracts, including all business transactions of the usual kind, are valid without being put in writing except when the Statute of Frauds, or some other statute of the state in which the contract is made, expressly requires that certain con-

tracts shall be in writing. The purpose of these statutes is to prevent fraud and perjury in cases open to an unusual degree to falsehood if the transaction were left to mere spoken words and to the memory of the parties and witnesses of what actually was said.

13. *Statute of Frauds*.—Enacted in England during the reign of Charles II, the Statute of Frauds has been reenacted with only minor modifications by the American commonwealths. It is a somewhat comprehensive code of rules some of which apply to contracts in general, but most of which apply to particular types of contracts. Thruout, its provisions are designed to insure readily provable evidence of the transactions in question. Generally speaking, this is adequate evidence in writing, tho in some cases, particularly in the case of the sale of goods of a specified value, other forms of evidence are declared admissible.

At this point we shall consider the main rules of the Statute which apply to contracts generally, and here we have to deal wholly with the requirements of written evidence. The provisions of the Statute which refer to particular types of contracts will be considered when those types are under consideration. Thus the provisions of the Statute which require written conveyances and leases of real property, and contracts in writing for the sale or leasing of an interest in land will be discussed in the chapter on the law of real estate. The requirements that contracts to answer for the debt or default of another must be in

writing will be treated in the chapter on the law of guaranty and suretyship; those relating to certain sales of personal property will be explained in the chapter on the law of sales of personal property. We shall now explain the other provisions of the Statute. The English Statute of Frauds has been followed, with certain variations in detail which will be noted hereafter, in all the states of the United States.

14. *Contracts not to be performed within a year.* One of the provisions of the fourth section of the Statute is that no action shall be brought on any agreement that is not to be performed within one year of the making thereof unless the agreement is in writing. The courts have uniformly construed this as meaning that a parol contract is good unless it *cannot* be performed within one year. A contract of personal service for two years, for instance, cannot be performed within the statutory period, and, therefore, must be in writing; but a contract to erect a building, which by the terms of the contract is to be completed in eighteen months, need not be in writing because it *may* be completed within a year. A fire insurance policy to run for two or more years is good tho not in writing because the loss by fire calling for completion of performance of the contract may occur within a year from the making of the contract.

15. *Contracts for indefinite periods.*—A contract

of service or other contract to be performed for an indefinite period, until the happening of some uncertain event, or as long as one of the parties continues in business, or during the existence of a corporation or of a partnership, need not be in writing because it may end within a year. For the same reason a contract to run for the life of one or both of the parties is good by parol. The death of either party which will terminate it may happen within a year.

16. *Contracts not to compete.*—A contract not to engage in business in competition with the other party for a period exceeding a year, by weight of authority, must be in writing. There are, however, cases holding the other way in Massachusetts and in some other states, on the ground that if the party died within a year the agreement would be fully performed, since the contract then would be at an end. But the same is true also of a contract of personal service for more than a year, since it ends in the death of either party, yet these are the very cases to which the Statute was intended to apply, and include by far the most important group in which the courts have held that the contract must be in writing under this provision of the Statute. In each case the party is relieved from further performance by death, since death makes further performance impossible.

17. *Method of performance.*—Tho parol agreements which may be performed within a year are

valid even if the parties fully expect, and the probabilities are strong, that their performance will take much longer, nevertheless the contract must be in writing if the method of performance as understood by the parties will *certainly* extend beyond a year, altho by abnormal and impracticable methods performances might be completed within the statutory limits. The understanding of the parties that a certain method of performance is to be followed which will certainly extend beyond a year brings the contract according to the best considered cases within this provision of the Statute.

18. *Contracts in consideration of marriage.*—The fourth section of the Statute also provides that no action shall be brought to charge any person upon any agreement made upon consideration of marriage unless the agreement is in writing and signed by the party to be charged. The usual case is an agreement for a marriage settlement in consideration of marriage or a promise to marry, or an agreement by the intended wife to give up property rights, such as dower, in consideration of the marriage. Such contracts must be in writing to be valid.

REVIEW

Define an infant as contemplated by law and his right to make and avoid contracts.

Describe the limitations upon right of contract which exists in cases of lunacy, drunkenness and, in the case of marriage, for women.

Discuss contracts made for the benefit of third parties.

Describe the nature and the general purpose of the Statute of Frauds.

Explain its provisions regarding contracts not to be performed within a year, and their interpretation.

Explain how the method of performance affects the validity of parol agreements.

CHAPTER VI

CONTRACTS—PERFORMANCE

1. *Conditions in contracts in general.*—Performance of contracts involves the carrying out of the promise or promises made for the benefit of the promisee, as limited by conditions (a) expressly imposed by the promisor for his protection, or (b) implied in fact from the circumstances of the case showing the intention of the parties tho not expressed in words, or (c) when implied by law for the promisor's protection because justice and expediency require them. Promises must be performed as made, or the promisor becomes liable to pay damages for breach of contract. If, however, he has qualified his promise by conditions which must happen before his obligation to perform the contract arises, he will not be liable unless it appears, not only that he has failed to perform his promise, but also that the conditions precedent, upon which his liability depends, have happened. Questions relating to the performance of contracts, therefore, apart from the obvious cases of interpretation of promises, are principally questions involving the different kinds of conditions, and their effect upon the liability of the parties for failure to perform their promises. The different kinds of con-

ditions in a contract will be now separately discussed.

2. *Express conditions*.—The promisor may make the performance of his promise subject to any condition he pleases, provided the condition does not call for an act which is illegal or impossible in the legal sense. The numerous conditions which are common in insurance policies are good illustrations. The purpose of the promisor is to limit his promise so that it will not bind him unless the condition happens. Frequently his purpose is to secure performance of some act which the promisee is to perform in consideration of his promise. By expressly making the performance of such an act a condition precedent to his own obligation to perform his promise, he may not only hold the other party liable for breach of his promise to do the act, but he may set up such failure as a breach of condition relieving him from his own obligation to perform his promise.

3. *Conditions implied in fact*.—Conditions implied in fact are true conditions intended by the parties to qualify their promises, tho not expressly made conditions in words; they are implied from the facts of the case. A contract to perform a personal service is necessarily subject to the condition precedent that the promisor continue alive for the period of the contract, and that he shall remain physically and mentally able to perform the service. A contract to sell goods is always subject to the condition that the buyer accept them. A contract to make repairs in a building necessarily involves the condition that

the promisor be allowed to enter and remain in the building for that purpose. These conditions do not differ in legal effect from express conditions. They are enforced because the parties presumably intended them, tho nothing was said about them in the contract.

4. *Conditions implied in law.*—Another group of conditions comprise those implied as rules of law regulating the performance of contracts and their enforcement, whose purpose is to do justice between the parties irrespective of their intent. A contract of sale of a chattel is a good illustration. Delivery of the thing sold and payment of the price at the time of delivery are mutual and concurrent conditions which the law implies, so that each party must offer to perform his part of the contract as a condition precedent to the obligation of the other party to perform on his side.

Justice demands that this rule be applied to the enforcement of such contracts. It may be said that the acceptance of this principle in business practice is so universal that the parties, in all such cases, may fairly be regarded as intending that their promises be limited by these conditions. Yet that would hardly seem to be material, as the law applies the rule whether they intended it or not.

Express conditions and conditions implied in fact must happen or be performed as the parties intended in order that the promisor may be held liable on the promise which they qualify. They are terms of his contract. He cannot be held liable except on the

contract as made by him narrowed by all the qualifications and conditions attached to it, irrespective of whether failure of the condition to happen or failure to perform it causes him damage or not. We shall see hereafter how the rule of substantial performance in certain cases has modified this principle.

5. *Performance prevented by promisor.*—If the promisor directly or indirectly prevents the performance of a promise to him or of a condition limiting his own promise, he cannot then set up this failure of performance either as a basis of recovery of damages in the first case, or as an excuse for non-performance of his own promise in the second case. It is thru his own fault that the other party has not performed.

To illustrate this, if a building contract provides that an architect's certificate of due performance of the contract to build shall be furnished as a condition precedent to payment to the builder of the sum he is to receive for erecting the building, and the owner prevents the architect from giving the certificate, he cannot set up the lack of the certificate as a defense to an action for the price. A buyer of goods, payment to be made on condition that they be delivered, cannot set up failure to deliver if he refuses to accept delivery.

In such cases, however, the promisee must show that he was ready, willing and able to perform the condition. If it appears that he could not or would not have complied with the condition in any event, whether the promisor prevented its performance or

not, he cannot recover on the promise, as in that case the prevention of performance of the condition by the promisor makes no difference. The usual case of this kind is a condition calling for the payment of money. If the promisor declares he will not perform his promise to which the payment is a condition precedent the promisee may hold him liable without paying or offering to pay as the condition requires, but it must appear that he was ready, willing and able to pay, otherwise repudiation of his promise by the promisor would make no difference.

6. *Waiver of performance of conditions.*—The differences between promises and conditions is clearly seen in the application of the law of waiver. An obligation arising from a promise cannot be waived; it must be discharged by act of the obligee in one of the ways hereafter discussed in the chapter on the discharge of contracts. A waiver cannot amount to a discharge of a contract, because a mere agreement to give up a contract without a valid consideration is void. But a condition is a mere limitation upon a promise which may be availed of by the promisor as a defense, and he may waive the defense either before or after breach of the condition.

7. *Waiver before time for performance.*—If the promisor says in advance that the promisee need not perform the condition, he cannot, after the time for performance has passed, set up the promisee's failure to perform the condition. To permit him to do so would be a manifest fraud. Thus a provision in a

building contract to the effect that the contractor could not recover for extra work or material unless ordered in writing was waived by a parol order for such work and materials and thru the acceptance and part payment therefor by the owner.

Notice of dishonor and presentment of a negotiable instrument may be waived in advance. The basis of the waiver in these cases is estoppel,¹ the promisee, having been led into a failure to perform the condition by the promisor's statement that he would not require such performance. Therefore, the promisor may withdraw the waiver if he does it while there is still ample time for the promisee to perform the condition, and he has not been led into changing his position by the waiver.

8. *Waiver after breach of condition.*—After breach of a condition precedent by the promisee the promisor may elect to treat the contract as tho no breach had occurred, or he may treat the contract as rescinded because of the breach of condition. The condition was reserved for his protection alone, and, if it will be more to his advantage to go on with the contract, he may do so by simply waving the breach of condition. It is like the right of a landlord to oust a tenant for breach of condition in a lease. The landlord may waive breaches committed by the tenant

¹ Estoppel is the name given to the rule that a man must stand by what he has said or done, on which another has acted in good faith and has changed his position, so that he would be damaged if the man estopped were allowed later to repudiate what he has said or done.

by any act recognizing the tenancy as continuing thereafter, as the condition is solely for his protection.

No question of a new consideration can fairly be raised in these cases; the original contract is not ended. The promisor's liability becomes subject to an accrued defense of which he may refuse to avail himself. However, he cannot take the position that the contract still continues for his benefit, and at the same time does not bind him because of the promisee's breach of condition.

9. *Conditions in the sales of goods.*—If a vendor delivers to the vendee goods which are defective, acceptance of the goods is a waiver of the breach of condition that goods of the quality specified in the contract be delivered. Therefore, the vendee must perform his promise to pay the price. By weight of authority this does not prevent him from offsetting the damage which he sustains because of the breach of contract by the vendor. Tendering defective goods is a breach of condition and of contract at the same time. Breach of the condition is waived by their acceptance, but acceptance is not a release of the vendor from liability to pay damages for his breach of contract unless the circumstances establish that the goods were delivered and accepted as full performance of the contract. The defect may be in the quantity or quality sold, or in the time of their delivery. The difficulties which have developed in

the law in connection with warranties will be discussed hereafter in the chapter on sales.

10. *Other illustrations.*—Failure to complete a building contract on time is both a breach of condition and of contract by the builder. An extension of time before default is a waiver of the first kind above discussed. After default by the builder, the owner may waive the breach by going forward with the contract, ignoring his right to rescind because of the builder's breach of condition, and he is liable for the price after the builder completes his work, with a right of set-off for the damages arising from the delay.

A contract to sell real property which cannot be performed by the vendor because of an incumbrance or other defect of title is another illustration. The purchaser may waive the breach of condition by accepting the title of the vendor and taking his deed. In this case however, he must pay the price without deduction of damages because the contract merges in the deed, and the vendee's only remedy will be for breach of covenant of title in the deed. He may get specific performance of the contract in equity, and in that case equity will deduct the amount of his damage because of the defective title.

Acceptance of defective workmanship is a waiver of the breach of condition that the work will be properly done, exactly as in the other cases above discussed. The work must then be paid for, with a de-

duction because of the defective workmanship; but if no complaint is made within a reasonable time, it is inferred that the performance as made was made and accepted in full discharge of the contract. No set-off will then be allowed.

If an employe breaks his contract and thereby gives his employer the right to discharge him, the act of continuing him in the employment with knowledge of his breach is a waiver of the right to rescind the contract and to discharge the employe. He cannot thereafter be discharged on that ground, unless the right to discharge him therefor is expressly reserved by the employer.

11. *Conditions requiring architects' certificates.*—We have seen that if the owner prevents the securing of an architect's certificate by a builder under a contract making the obtaining of such certificate a condition to payment of the price, the certificate will be dispensed with, e.g., the owner might induce the architect to withhold a certificate which ought to be given. If the architect dies or becomes incapacitated or refuses to act, it is generally held in the United States that the builder may recover the price without the certificate, it being the obvious intent of the parties that the condition shall apply only in the event that the architect can or will act. Performance of the contract may then be proved in other ways.

A more difficult question arises where the architect, acting in good faith, unreasonably refuses a certificate. In New York and several other states the

courts hold that the certificate may be dispensed with in such cases. In Massachusetts and probably a majority of the other states the opposite view is taken and the architect's decision is held to be final, except, possibly, in cases of gross negligence on his part. If the architect has acted in good faith without mistake as to the facts it is clear that his judgment of the matter should not be set aside for that of a jury and contrary to the express terms of the contract. However, if the architect's decision cannot be sustained on any reasonable basis, or is based on mistake of fact, it is clearly a case for relief on equitable principles, and the cases may probably be reconciled on that basis.

12. *Conditions as to time of payment of a debt.*—A sale of property, title passing at once, gives rise to a debt for the price, and an expressed condition that the price shall be paid upon arrival does not prevent recovery of the price in case the goods never arrive. Performance of the condition has become impossible, and it is clear that the parties had no such contingency in mind, the purpose of the condition being to fix a convenient time of payment. The literal terms of the contract are made to yield to the obvious intent that the debt should be paid in any event, title to the goods having passed to the purchaser.

13. *Substantial performance.*—If the promisee has substantially performed the conditions of the contract he may recover the contract price, tho he has

failed fully to comply with such conditions. The loss occasioned to the promisor by such failure is deducted from his recovery. Of course this is in violation of the express terms of the contract, and is justified as an interposition by the courts on equitable principles only to prevent a forfeiture of the promisee's labor and materials which would otherwise result. The promisee cannot get the benefit of this doctrine if his default has been wilful. Moreover, it must appear that the default is not serious so that no injustice is done the promisor by a deduction of damages arising from it.

14. *Conditions implied by law in bilateral contracts.*—For centuries covenants or promises given the one for the other were enforced by the courts as independent promises, each party having a separate and distinct action for a breach of the other's contract, subject to no defense because of his own failure to perform.

Lord Mansfield, in the latter part of the eighteenth century, introduced the doctrine of implied conditions. These conditions, having for their general purpose the requirement of the plaintiff in any such case to allege and prove that he had performed or offered to perform whatever he was bound to do under the contract prior to performance by the defendant, were based on the intent which the parties had or might have had if they had given the matter any thought. This was evidently a fiction used by the courts as a means to modify the old rule.

It is now generally recognized that, in the absence of expressed intent by the parties, the law will imply such conditions in bilateral contracts as justice demands in their performance, without regard to what the parties may have had in mind or might have intended if they had considered the matter.

15. *Failure of performance by one party relieves the other from his promise.*—Justice demands that a party substantially in default in the performance of his part of a bilateral contract shall not be permitted to hold the other party to performance of his part. The order in which performance of the respective promises of the parties is to take place is the most important factor in determining the liability of either party. When the contract or business custom provides that performance by one party is to precede performance by the other, such prior performance by the first party is implied by law as a condition precedent to the second party's liability to perform. The first party has broken his contract by his failure to perform the act which was to come first, and is liable in damages for the breach. The second party is relieved from his obligation to perform his part because of the breach of condition by the first party. Thus in a contract of service, performance of the service must precede payment therefor; if there is a failure to render the service as promised, the party in default is liable in damages to the other party, and has broken the condition implied by law that he perform. Thus the other party is relieved from his

promise to pay the price. Mere delay in performance by the party who is to perform first, of course, will not relieve the other party, unless it continues for such a time as to amount to a substantial breach.

Default in performance which is relatively unimportant is not regarded as a breach of condition. If the contract is for the sale of an automobile with two extra tires, and the vendor tenders the automobile with one tire only, the vendee is not discharged from his contract. He must pay the price less the value of the missing tire. The law implies the condition in these cases merely for the sake of accomplishing substantial justice, and the condition will not be implied where the result would be manifest injustice.

16. *When order of performance is not indicated.*—As in other cases, when the order of performance is not indicated, the plaintiff suing for breach of contract must show that he himself is not in default. For instance in a contract to refrain permanently or indefinitely from competition, for a price to be paid on a specified date, the party so refraining may sue for the price after the date of payment has passed; but he cannot recover if it appears that he broke his promise to refrain from competition prior to that date. If he has kept his promise to forbear, failure to pay the price for a time long enough to amount to a substantial breach of the contract will relieve him from further obligation to refrain from competition.

17. *Concurrent conditions.*—The law implies concurrent conditions not only in cases in which per-

formance on both sides is set for a fixed date, but also when no date is fixed, or when performance is to take place "on or before" a set day, if the promises on both sides are such that they can be performed at the same time. However, performance must be capable of being made at the same moment, as the delivery of a chattel or of a deed conveying land for payment of a sum of money. When performance on either side takes a period of time the condition implied will necessarily be precedent rather than concurrent. Cases illustrating implied conditions precedent in the preceding sections sufficiently illustrate this rule.

Express conditions in unilateral contracts as well as implied conditions in bilateral contracts may be mutual, and will always be so construed when performance may be concurrent at the same moment of time. Therefore unilateral offers to sell and convey land or to sell and deliver chattels in payment of a stated price are construed as calling for concurrent performance on both sides at the same moment, exactly as in the case of bilateral contracts to sell.

18. *Tender and readiness and willingness to perform.*—We have seen that in cases of express conditions the plaintiff must show either performance or tender of performance or that his performance has been waived or prevented by act of the other party, or again that the other party is unable or unwilling to perform his part of the contract.

The same principles apply to implied conditions. The tender of performance of concurrent conditions

is conditioned upon performance concurrently by the other party. If the plaintiff in such cases alleges and proves that the defendant has refused to perform his part of the contract, he need not make a tender which would be a mere form, but he must show that he was ready, willing and able to perform. If there is no tender and no refusal to perform by either party, neither can be held for breach of contract, since neither is in default.

If performance is to take place on a fixed date, and time is of the essence of the contract, tender must be made on that date; if time is not of the essence, tender must be made within a reasonable time thereafter, or the other party cannot be put in default. If no time is fixed for performance by the terms of the contract, then tender must be made within a reasonable time.

In other words the party suing must show that he has offered to do what his contract calls for as a condition precedent to holding the defendant liable for a breach of the contract. Here, as in cases of express conditions, tender need not be made when the other party has refused in advance to perform the contract, or has made performance impossible, as, for instance, by selling and transferring the goods or land to another person.

19. *Impossibility of performance of conditions not due to fault of the plaintiff.*—In case of impossibility of performance of conditions thru no fault of the plaintiff the defendant is relieved from liability exactly as tho the breach were due to the plaintiff's

act. The defendant has not received the thing or act he bargained for and therefore should not be compelled to pay. Illness of an employe, for this reason, frees the employer from payment of wages, as he has not received the employe's services. Failure to perform a contract for excavating or other construction will not be excused because of physical difficulties which make performance by the plaintiff impossible as a practical matter. The condition must be performed if he is to recover the contract price.

20. *Part or substantial performance.*—We have seen how in building contracts even express conditions will not bar a recovery by the builder if his failure to comply with the condition of performance is comparatively slight, and without bad faith. Where the breach of promise or condition extends only to part of the consideration, and the other party gets substantially what he contracted for, the breach of condition will not bar a recovery, and damages because of the breach will be deducted from the sum payable by the other party.

The application and enforcement of this principle necessarily depends in each case upon what justice demands. The contract may involve several promises by the plaintiff, and the one broken by him may be comparatively unimportant and incidental, or the breach may be a comparatively unimportant breach of the only promise made by the plaintiff. In such cases this doctrine of substantial performance applies.

On the other hand it will not apply and the plain-

tiff cannot recover if his breach is so important that it defeats substantially the main purpose of the contract, so that the defendant does not get substantially what he contracted for.

In addition to the building cases, this is further illustrated by the case of a plaintiff who contracted to cut and pile 50,000 cords of wood, the defendant agreeing to build shacks for his men. It was held that the defendant's failure to build the shacks was not such a breach of condition as would discharge the plaintiff from his promise to cut the wood.

21. *Time of performance*—*when time is of the essence*.—Failure to perform a promise at the time fixed by the contract is always a breach for which damages may be recovered. But is it also a breach of condition relieving the other party from liability under his promise? Under the cases mere delay in performance, if not unreasonably extended, is not treated as a failure to perform the condition unless time is of the essence of the contract. If time is made of the essence by express provision in the contract, then delay in performance gives the other party the right to rescind; time is also of the essence when the nature of the contract is such that time of performance is of primary importance to the promisor.

In these cases the same problem is presented as in other cases of incomplete performance. Does the promisor receive for the money which he is to pay substantially what he bargained for, so that justice will be done all around by merely deducting there-

from damages due to the delay, or is he deprived of the essence of what he bargained for because of the delay?

22. *Contracts of sale, time is of the essence.*—Executory contracts to sell personal property are subject to the rule that time is of the essence. Tender by one party to the other, either of the chattel or the price, must be made on the day fixed by the contract. In executed sales where title has passed, the rule is the other way. A reasonable delay by either party will not relieve the other from his promise. This is obvious in the case of sales on instalments, involving partial performance, and is justified in other cases of executed sales because title to the goods has passed to the purchaser.

Executory contracts to sell real property are subject to the same rules in this regard as similar contracts for the sale of personalty. Tender must be made by either party seeking to hold the other on the day provided for the delivering of the deed.

23. *Time is of the essence in other cases.*—Building contracts are generally held to come under the rule that time is not of the essence. Undue delay will amount to a total breach, but a delay which is not unreasonable will be remedied by a deduction of damages from the owner's payment. Here, as in other cases, time may be expressly made of the essence, and the facts of a particular case may justify such a holding.

In contracts of service time is not of the essence

unless expressly provided, even as to the time when performance is to start. But time is very important if the service is to be rendered in a commercial transaction involving the shipment or delivery of goods. Thus time of sailing is of the essence in a charter party.

24. *Severable or divisible contracts.*—A contract is severable or divisible when the performance on both sides is made up of distinct and exact parts, and parts of the price to be paid on one side are in return for corresponding parts of the goods or service to be supplied or rendered on the other. A contract of service for a year at \$100 per month payable monthly, and a sale of a specified quantity of coal to be delivered monthly at \$12 per ton, are illustrations. The distinctive feature of these contracts is that on performance of a specified part of the contract the amount agreed to be paid for that part at once becomes due and payable, irrespective of whether either or both parties are subsequently in default on later instalments.

A contract for the sale of a list of goods at prices stated for each item of the list is severable, so that on delivery of part of the goods and failure to deliver the balance the courts permit a recovery of the amount to be paid for the goods delivered, and damages for the failure to deliver the balance of the list. But no recovery will be allowed except on the delivery of all the goods if the contract so expressly pro-

vides or the intent to that effect is clear from the circumstances of the case.

Contracts of service for a stated period, as for a year at \$50 per month, nothing being said as to time of payment, have been quite generally construed as entire, so that the entire term of service must be rendered before the wages can be recovered. However, in Massachusetts and several other states it is held, more reasonably, that the reservation of wages by the month involves an implied intent that the wages be payable monthly so that the monthly wages which have accrued before the breach by the employe may be recovered by him, in spite of the subsequent breach of the contract on his part.

A material breach as to any instalment not only bars a recovery of the corresponding price or other performance as against the other party, but it gives the other party the right, unless the breach is waived, to terminate the contract as to the other instalments.

25. *Effect of prospective unwillingness or inability to perform.*—If one of the parties states in advance that he will not perform or makes such intention clear by his conduct, the other party may treat the contract as ended, and will be relieved from further performance. Inability to perform, arising from destruction of the subject matter of the contract, lack of title to the property to be transferred under the contract or other causes, will have the same result. Of course, prospective breaches of this kind will not

end the contract except as the other party so elects. He need not wait until the time for performance, however, but may rescind the contract and sue for damages.

REVIEW

Outline the three classes of conditions limiting the performance of contracts in general.

Explain what is meant by conditions implied in fact; conditions implied in law.

Define waiver and outline its effect when made after a breach of conditions.

Discuss the doctrine of substantial performance.

Explain the features of a severable contract.

CHAPTER VII

CONTRACTS—ASSIGNMENT AND DISCHARGE

1. *Nature of assignments of contracts.*—Under the ancient common law no right of action or right to enforce a claim in court could be assigned, at any rate without the consent of both parties to the transaction. A right of action was regarded as a personal thing between the immediate parties, and the right to enforce it could not be transferred to any other person.

The necessities of a slowly-developing commercial life required a departure from this extremely narrow and unwarranted position. The demands of business and business men resulted in the adoption into the English common law of the law merchant relating to commercial paper. Under this law negotiable bills of exchange and promissory notes could be transferred like chattels, title passing to the transferee and vesting in him like any other kind of property. Other rights of action in contracts not personal in their nature became assignable thru a fiction which regarded the assignee as the agent of the assignor with power to collect the amount due in the assignor's name but for his own benefit, and means were found, first in equity and later at law, to protect the assignee from any act of the assignor which would interfere with his

rights as owner of the contractual right. The courts still talk about assignments as powers of attorney to collect in the name of the assignor, but in most states the assignee sues in his own name in enforcing the claim and, of course, the amount collected by him is his. There is no doubt that the contractual right so assigned to him is his property, altho the old fiction still lives on in the rule that the technical legal title to the claim is not in him.

This is of practical importance in applying the doctrine in equity that a purchaser for value of any property without notice of any equitable right in a third person, takes free of the equity, provided he acquires the legal title. As the assignee of a contractual right does not get the legal title, except in the case of negotiable instruments, it follows that he takes as owner of the right subject to equities which may exist in third persons. This is a technical doctrine, for the lawyer rather than the business man.

2. *What contractual rights may be assigned.*—Accrued rights to the recovery of money, as in case of the price of goods sold, land conveyed, wages, or damages arising out of the breach of any contract, may be assigned freely. Personal contracts calling for a personal relation, as that of master and servant, cannot be assigned, tho wages already due may be assigned. The promisee cannot assign a contract with a painter to paint his portrait, tho he may assign the picture, just as the servant may assign his wages.

A contract to purchase goods or land, or the rights under any other contract not involving a personal relation may be readily transferred to a third person. Just as the results of personal service, such as wages, may be assigned, so also, may damages which have already accrued as a result of any breach of contract, whether personal or otherwise.

The strong tendency of the modern law is in favor of freedom of assignment. Contracts will be construed as permitting their assignment if at all possible. Therefore, a contract not to compete may be assigned with the business for the benefit of which the contract was made, as it is interpreted as being a contract not to compete with the business rather than with the owner of the business.

3. *How far future contractual rights may be assigned.*—It is clearly contrary to public policy to permit a man to assign away in advance whatever he may become entitled to in the future, and for that reason, the law in most states has set an arbitrary limit upon assignments of future contractual rights. There must be a contract under which the future debt may arise, whether a contract of employment or a contract of any other kind, in order that the assignment of the prospective and contingent debt may be valid. An assignment of future wages or future profits from an employment or business contract which the assignor hopes to secure is void, not because of anything in the nature of things which would prevent such assign-

ments but because they exceed the limit, fixed by the courts in the interests of public policy, beyond which these assignments shall not go.

4. *Assignments contrary to public policy.*—Apart from assignments forbidden by statute, such as claims against the United States until they have been allowed, it is generally held without the aid of any statute that the pay of public officers cannot be assigned in advance, tho cash wages or salaries which have become due may generally be assigned. Regarding options the better view is that they may be assigned like other non-personal contractual rights, in spite of the rule that an offer may be accepted only by the offeree. Pensions solely for past services are assignable, but pensions of soldiers and sailors in the United States are not subject to assignment because of statutory prohibition.

5. *Assignment of executory bilateral contracts.*—No difficulty exists as to the right to assign an accrued debt under a bilateral contract. But the complete transfer of an executory bilateral contract involves not only the assignment of the future rights of the assignor under the contract but also the delegation to the assignee of his obligation thereunder. Duties or obligations non-personal in their nature may be *delegated* to another but they cannot be *assigned*. The assignee who takes over such duties is bound by his express or implied promise to assume them, but the assignor of the contract continues liable for their performance to the other party to the contract. No

difficulty exists as to the assignment of the assignor's future rights under the contract, assuming they are not of a personal nature. But the only way in which the assignor may relieve himself of his obligations under the contract in such cases is by a *novation*, the formation of a new contract which is substituted for the old, the other party agreeing to release the assignor in consideration of the promise of the assignee to assume the assignor's obligations under the contract.

6. *Effect of express prohibition of consent to assignment.*—As the parties' intent controls in a contract, there can be no assignment if the contract forbids it. A prohibition of this kind is very unusual in ordinary business contracts not involving a personal service or other personal relation, and calling simply for the payment of money or the supplying of ordinary commodities. Sometimes a contract to purchase land and a carrier's contract to carry and deliver goods are expressly made non-assignable. Insurance contracts are regularly made non-assignable because of the change in the risk which might well follow an assignment of the policy before loss.

The delegation of duties under a bilateral contract may be forbidden in the same way. In letting a building contract the owner should bear in mind the possibility of assignment and delegation of duties thereunder to another builder. If the personal attention and responsibility of the builder in question is important, a provision forbidding assignment of the contract with the attendant delegation of duty

should be inserted in the contract. In many cases of this general nature the question is often a close one as to whether the contract may be assigned or not, and the doubt should be removed by an express provision one way or the other. So where a contract, because of its personal character, could not ordinarily be assigned, an express provision permitting assignment would make it freely assignable.

7. Distinction between assignments and orders, drafts and checks.—An order, draft or check calls for the payment to the payee by the drawee of the amount specified, irrespective of whether a debt or other claim exists against the drawee. There is no intent to assign a claim against the drawee in whole or in part. Even in the case of checks, tho nominally the check is drawn against a fund on deposit in the bank, it is an order to pay which may be honored irrespective of whether there are sufficient funds on deposit to meet it or not.

An order amounting to a partial or equitable assignment is illustrated by an order given by a builder to pay to another an instalment or part of it to become due under a building contract. A definite assignment of a part of the builder's prospective claim is clearly expressed in such case.

8. Form of assignments.—No particular form is necessary to the validity of an assignment. Even in the case of the assignment of instruments under seal, a parol assignment is good, except in Massachusetts where it is held that the assignment must also be

under seal. An assignment need not be in writing except where statutes so provide.

In some states statutes provide that, if the assignment be in writing, the assignee may sue in his own name; but that the assignment is good by parol, the writing being necessary only so that suit may be brought in the assignee's instead of the assignor's name.

In most states, however, the assignee may always sue in his own name by express statutory provision whether the assignment is in writing or not. Contracts for the sale of land must be in writing under the Statute of Frauds, and an assignment of such a contract must be in writing because it is not only an assignment of the contract but also a transfer of an equitable estate in the land which the assignor has acquired under the contract. The assignor alone can question the validity of the assignment in this case. The oral authority to enforce the contract in the name of the assignor as against the vendor is perfectly valid, so that the vendor cannot raise the objection of the Statute.

Assignments of leases have to be in writing under the Statute of Frauds. In New York and many of the states, assignments of leases for over a year must be in writing, while assignments of leases for a year or under may be by parol.

9. *Defenses which the obligor may set up against the assignee.*—As explained at the beginning of this chapter, in discussing the nature of assignments, the

legal title to the claim does not pass; all the assignee gets is a power of attorney to collect the claim for his own benefit. It follows that he takes the claim, subject to all defenses that the obligor has against the assignor, such as fraud, duress, and others, and also rights of set-off or counterclaim on other debts or obligations which under the local law might be set up by the obligor if an action on the claim had been brought against him by the assignor.

10. *Discharge of contracts.*—The usual and expected method of discharging a contract is by performance according to its terms. This phase of contract law has been sufficiently discussed in an earlier chapter. If the contract has been fully performed on both sides it is, obviously, at an end. The other ways in which a contract may be ended are by release, rescission by parol, accord and satisfaction, novation, rescission for breach of contract, cancelation, alteration, merger and impossibility. Each of these methods of discharge will now be separately discussed.

11. *Release of contracts.*—A release is a surrender of his rights by an obligee to the obligor. A release under seal effectively ends the contract. In states which have *not* abolished seals no consideration is necessary if a seal is used. In states which *have* abolished seals by statute or in which a seal is by statute made simply presumptive evidence of consideration, a release will have the effect only of a parol rescission, and a consideration is necessary.

In New York, the statute so providing applies only to executory contracts under seal, and as a release is not executory it has its original common law effect in discharging contracts.¹ A release of a right to arise in the future can be given effect only as a covenant not to sue, and as such it will accomplish its purpose as between the immediate parties, as the covenant will be perpetually enforced. But in the case of a future joint obligation, a release of one of the prospective obligors will not discharge the others because the covenant not to sue does not discharge the obligation when it arises; it merely bars an action against the obligor in whose favor it was made. A release of one of several joint obligors whose obligation is present, not prospective, will discharge all the others as well, unless the right to hold the others is expressly reserved, in which case it is construed as a covenant not to sue, and it will be enforced only in favor of the obligor in whose favor it was made.

12. *Rescission by parol.*—The ending of the contract by parol requires a new contract, and therefore, there must be a valid consideration to support it. In a bilateral contract, not fully performed on either side, there is no difficulty; the promise to give up performance on one side is consideration for the promise

¹ A release may be used in many situations. In the case of the payment of a debt for example, a receipt is merely evidence that the money has been paid. A release would go further and recite that in consideration of the payment made the debtor was released from all obligations of any kind growing out of the transactions which gave rise to the debt.

to give up performance on the other. The agreement will be implied from facts showing that the parties have mutually abandoned the contract, tho no agreement to that effect in words has been made. A new contract will be given effect as discharging a contract on both sides, so that each binds himself to something different, as a valid discharge of the old contract, the new one taking its place. This is not so, however, if either party under the new contract binds himself only to what the old contract bound him. He gives no consideration in that case for the new promise or promises made by the other party. The old contract may be in writing and the new contract may be by parol, unless a writing is necessary under the Statute of Frauds.

For the same reason a unilateral contract, or a bilateral contract which has become unilateral by performance on one side, cannot be discharged by mere mutual agreement without a new consideration. One party gives nothing in return for the other party's agreement to surrender his right to demand performance.

Contracts under seal at common law required an instrument under seal to discharge them. The modern law, however, is that an agreement by parol contract will be given effect as discharging a contract under seal. This is necessarily so in the many states which have abolished seals, and in the other states the same result is reached on equitable grounds.

13. *Accord and satisfaction*.—An accord is an

agreement by one party to give, and by the other party to receive, a stated sum of money or other thing of value in satisfaction and discharge of an existing right of action. The actual performance of that agreement is a satisfaction. The accord, however, cannot be set up as a defense to an action to enforce the original cause of action. The only relief against such an action is in equity for an injunction to restrain it, accompanied by an action for specific performance of the accord, tho few cases of the kind have been decided. If the accord is performed, that is, if the agreed amount is paid and accepted in satisfaction of the cause of action, it is a complete defense to the enforcement of the claim. An accord alone may be intended as satisfaction, the promise to pay the amount of the accord taking the place of the original obligation, but such a case is unusual, and the facts indicative of such intent must be clear.

The requisites of a satisfaction are the same as those of consideration. The adequacy or inadequacy of the satisfaction is immaterial, the courts leaving to the parties the determination of their own bargain. Payment of part of an undisputed debt is not a good satisfaction, and any other act which would be held insufficient as consideration for a promise will also be insufficient as a satisfaction. The tests of a valid satisfaction and valid consideration are, therefore, the same.

14. *Attempted satisfaction of disputed claim by check.*—A check sent in full satisfaction of a disputed

claim, a statement to that effect being sent with the check or written upon it, followed by a reply from the creditor that he will apply the check on account but will not accept it in full payment, is generally held to be a good accord and satisfaction since the creditor cannot keep the check without accepting the terms on which it was sent to him. A few courts have held that no satisfaction occurs in such cases unless the parties so intended, and obviously, no such intent exists in the creditor. These cases have been overruled in New York, Massachusetts and some of the other states by later cases. In the above case the creditor cannot assert that he has converted the check when his only right to keep it is in satisfaction of his claim.

The prevailing rule that a satisfaction occurs is based on the general principle that a man cannot assert that an act was done wrongfully when it may be done rightfully with the result of binding him to some obligation. A tenant holding over at the end of his term is liable as a hold-over tenant even tho he gave notice before holding over that he did not intend to be bound for another period.

15. *Accounts stated*.—An account stated is a statement of account between the parties fixing a stated sum as the amount due, based on a prior debt or debts, which the debtor expressly or impliedly agrees to pay. The new promise takes the place of and operates to discharge the debt or debts on which the account stated is based. The creditor's action is brought on

the account stated, and the items of indebtedness need not be set forth or proved in the action.

The more usual form of an account stated is where the creditor submits a statement of account which is retained by the debtor without objection for an unreasonable time. There need be no consideration, other than the prior indebtedness, for the promise to pay the amount stated. This is probably a survival of the old law that prior indebtedness was a good consideration for a promise.

16. *Novation*.—A novation is a new promise made by a third party to pay or assume an existing obligation in consideration of the discharge of the original obligor. The original obligation is discharged by the obligee in consideration of the promise of the third party to perform it. For instance, a tenant assigns his term to X, and it is agreed between the landlord and tenant and X that the landlord shall release the tenant from his obligation to pay rent thereafter in consideration of X's promise to pay rent directly to the landlord. The consideration for the agreement of the landlord to discharge the tenant from his obligation is the assignee's promise to pay the rent to him. It is, of course, evident here that a new and distinct contract must be made, and that the creditor, as well as the debtor and the third person, is a necessary party.

An agreement by the assignee in the above case to pay the rent in consideration of the discharge of the tenant, but without the concurrence of the landlord,

would not discharge the tenant, tho the assignee would become liable to the landlord as a third party beneficiary.

17. *Rescission for breach of contract.*—What constitutes a breach of contract thus giving the other party the right to end the contract and sue for damages, or at his election, to waive the breach and proceed with performance of the contract, has been made clear in the chapter on performance of contracts. If the contract is rescinded for breach, it ends at once, leaving only an action for damages against the party guilty of the breach.

18. *Cancellation.*—Cancellation and surrender are the usual means of discharging contracts under seal and negotiable instruments. Such instruments have always been something more than mere written evidence of contracts; they are the actual contracts, and their surrender and cancellation results in their discharge. In the case of negotiable paper surrender alone before maturity with intent to discharge, while a good discharge as between the parties, will not be effective as against an innocent purchaser for value in case the instrument is wrongfully transferred to him before maturity by one having apparent title as payee or indorsee. The surrender in such case is an equitable defense which is cut off by a transfer to a purchaser for value without notice.

Surrender of a simple contract in writing has the effect only of evidence of discharge by a parol contract, and whether or not a valid contract or discharge

has taken place will turn on the principles previously discussed in this chapter.

19. *Alteration*.—A material alteration of a written contract, whether under seal or not, if fraudulently made by the obligee, vitiates the contract. But the contract is not destroyed thru an alteration made by mistake, or with no fraudulent intent. Immaterial alterations have no effect irrespective of motive or intent. Alterations made by the obligor will, of course, not avoid the contract. Alterations made by a stranger, or by the agent or attorney of the obligee without authority from him, do not avoid the contract.

The Uniform Negotiable Instruments Law has modified the rule in its application to negotiable instruments. By copying the corresponding provision of the English statute, the English rule of discharging the instrument if altered by a stranger while it is in the possession of the obligee, or if altered by the obligee himself or by his agent, without fraudulent intent, has apparently been established by this statute in the many states which have enacted it.

20. *Discharge of contracts by merger*.—When a judgment is recovered on a contract obligation the contract merges in the judgment. So also when a contract under seal is made and delivered between the same parties to take the place of an existing simple contract, the simple contract is discharged by merger in the specialty.

The same result follows the giving of a negotiable instrument (bill or note) in discharge of his debt by

the debtor to the creditor. The intention to discharge the debt must appear affirmatively. If it does not so appear, then the law presumes that an absolute discharge of the debt was not intended. The action on the debt is suspended until the bill or note matures, and if it is then dishonored the debt is revived and the bill or note is treated as security for its payment.

21. *Impossibility of performance.*—Subjective impossibility, arising from the inability of the promisor to perform, as his insolvency, does not relieve him of his obligation. Objective impossibility, where performance is impossible because of some condition not depending upon the capacity or resources of the promisor, will relieve the promisor from his contract in several classes of cases. It will be helpful to discuss briefly these cases.

(a) When by change in the law the act contracted to be done has become illegal the promisor is relieved from his contract. It is clear that a party cannot be required to break the law, and the justice of declaring the contract at an end in such a case is obvious.

(b) Again, when performance of a contract involving personal service has become impossible by the death or continued illness of the party who was to perform, this will serve to terminate the contract. The death or illness of the employer will also end the contract if his relation with the employe was a personal one. But in contracts of employment, in spite of a tendency of the cases to hold that the death of

either employe or employer will end the contract, there is no good reason why the employer's death should have that effect when the situation is such that supervision over the employe was or could be delegated to some superintendent or foreman. In many cases of contracts of employment the employer's contract is not personal in its performance, tho the employe's always is. The illness of the employe must continue beyond a reasonable time before the employer can terminate the contract on that ground.

(c) Destruction of the subject matter of the contract is another case falling in this same general category. A contract to sell a specific chattel or chattels necessarily involves their continued existence. Their destruction, therefore, ends the contract. If some of the goods are destroyed or seriously damaged the buyer may elect either to rescind or to take what is left and pay for them the pro rata sale price if the contract was divisible, otherwise he must pay the full price. For the same reason destruction of a building or ship essential to the performance of the contract discharges the contract. Thus the owner of a cheese factory was discharged from his contract to manufacture cheese from milk supplied by farmers in the neighborhood by the burning of his factory.

On the other hand, a contract of employment to sell the employer's products manufactured in his factory was not discharged by the burning of the factory. It is evident that the impossibility of performance

which relieves the parties must arise from such an important change in the situation connected with performance of the contract that the parties could not reasonably have intended that the contract should continue under such new conditions.

The usual way of explaining the different cases of impossibility of performance arising after the contract is made is that a condition is implied in fact, based on the reasonably presumed intent of the parties, that the person or thing essential to performance will continue in existence so that performance may be made. Either the use of the factory, ship, stream, or other means of performance must have been contracted for or such use very clearly understood by the parties as the sole means of performance in order that a condition of this kind will be implied. A sale of goods not identified, or a contract to manufacture goods without specifying the means of manufacture will not be discharged because the contractor's goods or the factory with which he intended to fulfil the contract have been destroyed.

Impossibility arising because of inability of the promiser to carry out his contract, subjective rather than objective, has no effect on the contract. His insolvency or inability to raise the amount required to pay the price, or the practical impossibility of securing the goods which he has contracted to deliver because of market conditions or otherwise will be no excuse, because, obviously, he assumed the risk, and no such condition could be fairly implied. In the

case of a building contract, destruction of the building before completion by fire, tempest or otherwise without fault of the builder, does not discharge him from his contract or extend his time for performance, and for the same reason obstruction in performing a contract for excavating will in no way modify the contractor's liability.

REVIEW

What is an assignment? Explain why the old rule that contracts could not be assigned has been modified, and what the present tendency in this respect is.

Distinguish between assignable and nonassignable contracts, giving practical illustrations of each class.

Explain how the exercise of the right of assignment may be prevented, and the circumstances in which it may be desirable to do this.

Name the various ways in which a contract may be discharged

Define a satisfaction and tell what are its requisites.

Explain "novation."

State the rules of law regarding alterations in contract, and regarding impossibility of performance.

CHAPTER VIII

Negotiable Instruments

1. *Origin of negotiable instruments.*—Negotiable instruments include promissory notes, bills of exchange and checks. There are other instruments which have some of the qualities of such commercial paper and are sometimes described as quasi-negotiable instruments. Bills of lading, certificates of deposit, warehouse receipts, stock certificates, coupons and letters of credit are examples of this type.

The law of negotiable instruments illustrates strikingly the historical fact that much of the law is little more than an enunciation by courts, in the form of decisions, or by legislatures, in the form of statutes, of certain usages, customs and principles of conduct which have grown gradually to be generally accepted by the community before being reduced to written statutes and rules binding upon each member.

The law of negotiable instruments originally grew up as a custom among the merchants of London. Because of its convenience in the transaction of business this custom finally came to have the force of law, its rules were enforced by the courts and finally crystalized into a statute adopted by Parliament in 1705. That statute served as the basis of the American law upon the subject until the Uniform Nego-

tiable Instruments Law was prepared. In the last twenty-five years this law has been adopted by most of the states.

2. *Negotiability*.—Negotiable paper is of great convenience to the business man. The quality of negotiability enables the owner of the instrument to transfer to another person a greater or more valuable right in the instrument, or a better title to it than the original owner himself possessed.

When a party to an ordinary contract assigns his rights under the contract, or as we say, assigns the contract, the assignee is in legal effect substituted in place of the original party. The assignee assumes entire liability on the contract. Any defense or counterclaim which would have been available as against the original party to the contract is equally good against the assignee. Thus the rights and obligations of the assignee of a contract become impossible of determination without a full inquiry as to the rights and obligations existing between the original parties to the contract.

The quality of negotiability, however, enables the holder of a promissory note or bill of exchange to transfer the title to the instrument to another person free from all such defenses, set-offs and counterclaims. In consequence the party under obligation to pay is compelled to pay in exact accordance with the terms of the instrument regardless of any claim that he might have against the original holder of the instrument.

Suppose that Brown buys from Sharp a bill of goods which Sharp has warranted to possess certain qualities and gives Sharp a negotiable note in payment for the goods. Later Brown discovers that Sharp's warranty as to the quality of the goods is false and fraudulent. If Sharp brings action against Brown on the note, Sharp's fraud could be used by Brown as a complete defense to the action.

But, if instead of holding the note until it became due, Sharp discounts it at his bank or transfers it in the usual course of business to Smith, who is ignorant of the fraud by which Sharp procured the note, the bank or Smith could compel Brown to pay the note in full regardless of the fraud. Brown could claim redress only from Sharp. Negotiability thus enables such instruments to pass from hand to hand by indorsement, or sometimes by mere delivery, similar in many respects to paper money.

To illustrate another advantage of negotiability, suppose in the above case that Brown had merely purchased the goods from Sharp on sixty days' credit without giving any note for the amount and Sharp thereafter had assigned the claim to Smith, who, shortly after the term of credit has expired, demands payment from Brown only to find that Brown, in ignorance of Sharp's assignment to Smith, had paid the amount to Sharp on the day it fell due. Such payment by Brown would be a complete defense to any action that Smith might bring against him and Smith would be left to seek redress from Sharp.

Smith might have protected himself by giving immediate notice to Brown that he had acquired the claim from Sharp.

However, where a *negotiable instrument* is transferred, the transfer is complete and full title passes to the transferee *without notice* to the debtor. When a debtor discharges his obligation under such an instrument, he must see to it that the person receiving the money is the holder of the instrument. In fact the debtor is entitled to and should insist upon the surrender of the instrument at the time he pays it.

3. *Negotiability of promissory notes.*—A promissory note or bill of exchange may or may not be negotiable. Whether it is negotiable or not can always be ascertained by looking at the instrument. To be negotiable, the instrument must contain so-called “words of negotiability.” If, in the above case, Brown had made his note payable simply to John Sharp, the note would not have been negotiable, but if he had made the note payable to “John Sharp *or order*,” or the note had read “I promise to pay *to the order* of John Sharp,” or had read “I promise to pay *to bearer*,” the note would have been negotiable. Thus the words, “to order” or “to bearer,” are words of negotiability and determine the negotiable quality of the instrument.

What has been said as to negotiability applies equally to bills of exchange and promissory notes. These two instruments have many other qualities in common which will now be considered, but for the

ment to Albert Hoe, and delivers it to him, the payee will then be known as an *indorser*, and Hoe would be described variously as the *indorsee*, *owner* or *holder*.

Business usage has sanctioned certain definite forms for notes, drafts and other instruments and it is the part of wisdom for men in business to insist that all instruments follow the customary forms. The fact that irregular and informal instruments may in some cases serve the same purposes is no excuse for slipshod business methods. However valid in law, such irregular instruments are always questioned in practice. If the use of these irregular instruments is not to be commended, it is none the less important that the business man should know his rights under them when, thru the ignorance of his customers or the negligence of his employes, they come into his possession.

5. *Formal requisites of negotiable instruments.*—An instrument to be negotiable must conform to the following requirements:

- (a) It must be in writing and signed by the maker or drawer
- (b) It must contain an unconditional promise or order to pay a certain sum of money
- (c) It must be payable on demand or at a fixed or determinable future time
- (d) It must be payable to order or to bearer
- (e) Where the instrument is addressed to a drawee, he must be named or otherwise indicated therein with reasonable certainty.

As these requirements are of the greatest importance, we shall have to consider them somewhat in detail in the order in which they are stated above.

6. *Instrument must be written and signed by maker.*—A written statement, signed by the maker, to the effect that a certain amount is due a person named, implies that the money is due from the maker. It is an acknowledgment of indebtedness which implies a promise to pay the indebtedness on demand. Such an instrument is a promissory note. In a few states, including New York, an instrument in the following form, “I O U one hundred dollars” has been decided to be a promissory note payable on demand, but in other states the courts have held that such an instrument was a mere acknowledgment of indebtedness and created no *new* obligation to pay.

Should the instrument, however, read “I O U *or bearer* one hundred dollars,” or “Due John Mason *or order* one hundred dollars,” or “Due John Allen ninety-four dollars *on demand*,” the instrument in each case would be treated as a promissory note despite its informal character. This is the case since the law would imply from the words, *or bearer*, *or order*, or *on demand*, a *new* obligation to pay at a particular time or in a particular manner.

The advantage to the creditor of obtaining a *new* obligation from the debtor can be shown by considering the case of a coal dealer who at various times thruout the winter delivers coal to a customer upon an order received by telephone and who during the

following summer finds it necessary to sue the customer for the purchase price. In order to prove his case against the customer, it would be necessary for the coal dealer to prove the actual delivery of each load of coal. His drivers would probably not remember these particular deliveries and so could not testify to them. The defendant's employe who received the coal might find it to his interest to have a still shorter memory. If receipts were taken by the driver, it would be necessary for the coal dealer to prove the genuineness of the signature on each receipt and that it was signed either by the customer or by an employe who was authorized to so sign. The coal dealer might lose the case because of the difficulty of proving delivery.

If, on the other hand, the coal dealer had had the foresight to obtain from his customer a promissory note for the amount due and it then became necessary to sue the customer, the coal dealer would sue, not upon his original claim for the coal, but upon the promissory note. In that action it would be necessary for the coal dealer to do no more than produce the note and prove that the signature of the maker of the note was the defendant's signature.

7. *Unconditional promise.*—It is essential to negotiability that the instrument should be payable absolutely, that is, that the question whether or not the time for payment has arrived shall be determinable from a mere reading of the instrument without ascertaining from any extrinsic source whether or not some

condition has been fulfilled. For instance a promise to pay "thirty days after the maker shall marry" or "one year after date if I am then living," or "30 days after the ship *Franconia* arrives at New York," is a *conditional* promise. The holder of such a promise could not decide merely by reading the instrument whether or not the time had arrived for payment. Such an instrument might be a valid contract, but it would not be a negotiable promissory note.

8. *Certainty as to amount.*—The note must be a promise to pay a fixed sum of money which is legal tender at the place where the note is given. A promise to pay a fixed amount in foreign money or in bonds or in wheat, altho it might bind the maker to the fulfillment of his contract, would constitute merely a contract, not the special kind of contract known as a promissory note. But it does not destroy the character of the instrument as a promissory note to mention the *kind* of money, such as "in gold coin" or "in bank bills," so long as the money named is legal tender at the place of payment. Nor is the note defective because of uncertainty of the amount if it provides the payment of a specified sum "with exchange on Paris" or "with interest."

It is also possible without violation of the rule as to uncertainty to provide that the amount shall be payable in specified instalments at specified dates, and the note may also provide that upon failure of the maker to pay any instalment the holder of the note

shall have the option of declaring the entire amount due and payable at once.

9. *Time must be fixed or determinable.*—If the time of payment fixed by the instrument is certain to arrive altho the precise time may be uncertain, the requirement as to time is sufficiently met. An example of this is an order or promise made by an individual to another to pay a certain sum of money “60 days after my death.” Since the maker is certain to die, the law is fulfilled.

Where a note fixes no specific time for payment, or where it expressly states that the maker will pay a fixed sum “on demand,” it is called a demand note and the holder may demand payment at any time, even on the same day that the note is given.

So far as the liability of the maker goes, payment of such a note may be demanded at any time before the Statute of Limitations has run against it (in most states, six years) but in order to hold the indorser liable upon such a note, payment must be demanded within a reasonable time. In determining what is a reasonable time, the usage of trade or business with respect to such instruments and the facts of the particular case must all be considered.

10. *Parties must be identified.*—The requirement regarding the use of “or order” or “bearer” has been discussed under the head of negotiability and needs no further elaboration here. Not only the drawee but all parties to the instrument must be designated

with sufficient certainty for their identification. The name or signature which a person customarily uses may be employed to identify him as a party to such an instrument. For instance, William Brown may sign with a mark or merely by his initials, and if he conducts a store under the trade name, Lucile, he may be designated by that name without impairing the legal effect of the instrument.

A bill was held good which bore no designation of the drawee except the words, "Payable at No. 1 Wilmot Street, opposite the Lamb, Bethnal Green, London," it appearing that the bill had been presented to Charles Milner who lived at that address and had been accepted by him. But had Milner declined to accept it doubtless the bill would have been treated as a nullity, because of the insufficient designation of the drawee. Generally speaking, the entire omission of any element of such an instrument, for example, the amount to be paid, the promise to pay or the person by whom or to whom the money is to be paid, renders the instrument a nullity.

Bills and notes are sometimes intentionally made payable to the order of a purely fictitious payee or non-existing person. For example, "to cash," "to profit and loss," "to the man in the moon." Such instruments are treated as payable to bearer and title passes by mere delivery of the instrument without indorsement.

11. *Collateral notes.*—A negotiable note may contain a statement reciting that collateral security has

been given by the maker, specifying the property or securities and authorizing their sale in case the instrument is not paid at maturity. It may contain a clause authorizing the maker to sell the collateral and regulating the manner of selling if the note is not paid at maturity. It even may contain a promise to pay the costs of collection and the attorney's fees.

12. *Omissions and blanks.*—The validity and negotiable character of a bill or note are not affected by the fact that the date or the words, "value received," are omitted, nor by failure to state that any value has been given for the note. It is optional to designate a place where the note shall be payable, as "at the First National Bank of New York," or "at my residence in Greenvale."

Sometimes a note, check or bill of exchange is delivered by the maker in an incomplete form with one or more spaces left for the insertion of an important part of the instrument. In such a case the holder has authority to fill the blank in accordance with the understanding of the parties; if he fills it for a different amount or contrary to the agreement, he cannot enforce it against the maker. But if he then indorses and delivers it for value in the usual course of business to a third person who has no knowledge of the agreement under which the holder received it, the third person can enforce it against the maker.

Thus, if Brown sends Crooks to buy goods and gives him a promissory note payable to the expected

seller of the goods but leaves a blank space for the amount of the note with instructions to Crooks to fill it by writing in the purchase price of the goods, not exceeding a certain amount, and Crooks fills the space with greater amount and obtains a loan for that amount from the merchant instead of purchasing goods from him, the merchant, if ignorant of Brown's instructions, can compel him to pay the larger amount regardless of what Crooks may have done with the money.

However, if Brown should write his name on a blank paper, as a specimen of his signature, and give it to Crooks and the latter should write a note or a check over the signature and transfer it to Green for cash, Green could not enforce it against Brown, altho he took it without knowledge of the fraud of Crooks, for in that case Brown never intended to entrust Crooks with a negotiable instrument, even an incomplete one. Even if the merchant knew that the instrument had been delivered by Brown in an incomplete condition, he would still have the right to assume, in the absence of knowledge to the contrary, that Crooks had authority to fill the blank as he saw fit. Such cases are governed by a fundamental rule of law of general application to the effect that where one of two persons, both of whom are innocent of any wrong, must suffer thru the fraud of another, the loss should fall upon him whose *negligence* or misplaced confidence in the honesty of the wrong-doer has given the wrong-doer his opportunity.

Sometimes a man engaged in business prepares an incomplete negotiable instrument and leaves it in his desk ready for use at a subsequent time. In such case, if an employe finds the instrument, fills in the amount and negotiates it, even the bona fide holder will not be able to enforce the instrument against the maker, for the instrument was never delivered by the maker, and leaving it in his own desk or office in an incomplete form is not regarded as a negligent act.

13. *Interest*.—A note or bill does not bear interest unless it so states, but if a note by its terms is payable “with interest” or “with use” it bears interest at the highest legal rate in the state where it purports to have been made, i. e., the place named in the date of the note. For example, a note which is dated, New York, May 1, 1920, purports to have been made in New York on that date.

It is the custom for banks to deduct interest in advance, computed on the face value of the note. Thus, if Brown borrows from his bank \$10,000 for sixty days at 6 per cent interest, the bank upon receiving his note retains \$100 and credits him with \$9,900. Of course, the result is that the bank actually gets more than 6 per cent for the use of the money loaned to Brown, but even in those states where the highest legal rate of interest is 6 per cent, such a transaction is not regarded as usurious. When a non-interest bearing note is payable on demand, legal interest starts at time payment is demanded. Where a non-interest bearing note is payable at a

fixed date, interest at the legal rate begins to run upon the note after the date upon which it is payable.

14. *Consideration*.—Like any other contract, a promissory note, as between the maker and payee, must have been issued for a valuable consideration. Consequently, lack of consideration is always a good defense for the maker against the payee. But if the note is negotiable, it differs from other contracts in that it is implied without proof that it was issued for a valuable consideration and every person whose signature appears upon the note is deemed to have become a party thereto for value. Therefore, the fact that the note was made or transferred without consideration is no defense to an action to compel payment of the note which is brought by a subsequent holder of the note who, in the usual course of business, has given value therefor, in ignorance of the fact that the note was originally issued without consideration. Such person is usually described as a *bona fide holder* or a *holder in due course*.

Any consideration which will support an ordinary contract will support the making or transfer of a bill or note. What constitutes a sufficient consideration for a contract has been explained in a previous chapter.

The words, "value received," when appearing in a note or bill are simply an acknowledgment that a consideration has been received by the maker or drawer. But the instrument itself implies that a consideration has been given and the presence of the

words, "value received," does not prevent the maker or drawer from proving that there was, in fact, no consideration for the instrument. Therefore the phrase has no effect and is useless.

REVIEW

Name the common negotiable instruments.

Explain the difference between negotiability and assignability.

State the requisites of a negotiable promissory note; of a bill of exchange.

Explain what is meant by "unconditional promise"; "certainty as to amount"; "fixed or determinable future time."

Outline the law as to omissions and blank spaces in negotiable instruments.

States the law as to consideration for negotiable instruments.

CHAPTER IX

PARTIES TO NEGOTIABLE INSTRUMENTS AND THEIR OBLIGATIONS

1. *Liability of maker.*—The maker of a negotiable note promises to pay it according to its terms to the legal holder upon its presentment and surrender, either upon the day of its maturity or later. His liability differs from the ordinary liability on a contract in that, if the note does not state the place of payment, the holder must seek the maker at his residence or place of business, while in the case of an ordinary debt it is the duty of the debtor to seek the creditor for the purpose of paying.

Furthermore, in the case of an ordinary debt the debtor has until midnight of the date of maturity in which to pay, but in the case of a negotiable instrument the maker must be ready to pay at any time that the holder may present the instrument during business hours if it is payable at a bank or place of business, or between the hours of rising and retiring if it is payable at the maker's residence.

The maker of a note also agrees that should the note be paid by one of the indorsers, the maker will reimburse the indorser. Unlike an indorser, the maker is not relieved from liability upon the note by failure on the part of the holder to present the note to the maker and demand payment on the date of its

maturity. Whether or not the maker becomes liable to any one except the payee depends upon whether and to what extent the note has been indorsed.

2. *Kinds of indorsement*.—A note made by William Brown to the order of John Sharp could be indorsed by Sharp by writing his signature either upon the instrument itself or upon a paper attached to it, either with or without additional words. It is customary to write the indorsement upon the back of the instrument. If the instrument is payable *to bearer*, title to it, as previously explained, may be transferred from one person to another by mere delivery of the instrument, but if it is payable *to order*, title can be transferred only by the indorsement of the payee, in addition to the actual delivery of the instrument.

Moreover, a negotiable instrument must be transferred in its entirety. An attempt to transfer a part only of the amount payable is a nullity, altho, of course, where an instrument has been paid in part, it may be indorsed as to the residue.

The business man should be familiar with the effect of the following ordinary forms of indorsement:

- (a) Blank indorsement
- (b) Special indorsement
- (c) Restrictive indorsement
- (d) Indorsement without recourse
- (e) Conditional indorsement.

Let us explain these in detail.

3. *Blank indorsement*.—The simple signature, “John Sharp,” on the back of the note is called a *blank* indorsement. It specifies no payee and consequently an instrument so indorsed becomes payable to bearer and may subsequently be transferred from hand to hand in the usual course of business by the mere delivery of the instrument. Of course, if an instrument so indorsed should be lost or stolen, there would be no legal delivery; hence the finder or the thief could not recover upon the instrument for he would have no title thereto. But should the finder or thief in his turn transfer the note to a bona fide holder, the latter could enforce the note against the maker.

4. *Special indorsement*.—The words, “Pay Ray Smith” (Signed) “John Sharp” on the note originally made out to the order of Sharp constitute a *special* indorsement because it specifies Ray Smith as the person to whom or to whose order the note is to be payable. The indorsement of Ray Smith would then become necessary to the further transfer of the instrument. Contrary to the common belief it is not necessary for Sharp to use words of negotiability in his indorsement to Smith because since the note is originally negotiable, it will continue so until its negotiation is restricted by specific direction. Therefore, it is immaterial whether the special indorsement reads “Pay to Ray Smith” (Signed) “John Sharp” or “Pay to the order of Ray Smith” (Signed) “John Sharp.”

On the other hand, let us suppose that we have an instrument which on its face is payable to bearer and on which a special endorsement, such as "Pay to Ray Smith" (Signed) "John Sharp" is placed. Such an instrument would continue to be transferrable by mere delivery and any holder acquiring it in the usual course of business could enforce it against the maker, but no subsequent holder could enforce it against Sharp or Ray Smith unless Ray Smith had indorsed and delivered the note and then only in accordance with the terms of Ray Smith's indorsement. The reason for this rule is that Ray Smith by becoming an indorser could be held liable only in accordance with his contract of indorsement, and since he is the holder and absolute owner of the instrument he has the absolute right to specify to whom payment shall be made, or to attach any conditions he may desire to his liability upon the instrument.

5. *Restrictive indorsement*.—An indorsement is restrictive which either:

- (a) Prohibits the further negotiation of the instrument
- (b) Constitutes the indorsee the agent of the indorser
- (c) Vests the title in the indorsee in trust for or to the use of some other person.

In the case of such restrictive indorsements as "Pay Ray Smith only," "Pay Dewey and Hunter for collection," "For deposit in the Mercantile Trust Company," it clearly is the intention of the indorser to exercise some sort of control over the proceeds of the

bill or note. Every person to whom a negotiable instrument is transferred is charged with the duty of examining the instrument and must at his peril take notice of any limitation upon the indorsee's right to dispose of the instrument. A person to whom an instrument is so indorsed acquires the legal title to the instrument and may sue in his own name to collect the instrument or take any other action in his own name to accomplish the purposes for which the instrument was indorsed to him as expressed by the indorsement. His dealings, however, are restricted to those purposes.

The indorsement, "Pay to Ray Smith for the use of Marie Smith," also gives Ray Smith legal title to the instrument and enables him to bring suit to collect it, but it is notice to the world that Ray Smith holds the note and its proceeds in trust for Marie Smith. Ray Smith can in turn indorse this instrument and deliver good title to his indorsee so long as he is acting apparently for the benefit of Marie Smith. But if he attempted to transfer the note in payment for goods sold to himself or services rendered to him individually, the purchaser would be charged, by the terms of the indorsement, with notice that Smith was abusing his trust. The purchaser would not get good title to the note nor would the maker of the note be justified in paying the note to anyone except Smith.

For the same reason it is not safe to take a check or note signed in the partnership name for goods

sold or money loaned to a partner for his own personal use.

6. *Indorsement without recourse*.—The words, "Pay Ray Smith without recourse" (Signed) "John Sharp," would constitute an indorsement *without recourse* to the indorser. Its legal effect is that Sharp transfers all his rights in the instrument to Smith, but that Sharp assumes no obligation whatever to Smith or to any subsequent holder of the note, except to warrant that the instrument is genuine, has not been forged or altered, that he has good title to the instrument, that all parties to the instrument are competent and that he knows of nothing to render it invalid. But he does not agree to pay the instrument in case the person originally liable upon it fails to pay.

7. *Conditional indorsement*.—Such indorsements as the following, "Pay to Mary Smith when she arrives at twenty-one years of age," "Pay to Dewey and Hunter when the ship Franconia next arrives at New York," are *conditional*. If an instrument were originally made payable upon such a condition, its negotiability would be destroyed, but where the bill or note as originally made contains words of negotiability, such an indorsement is held not to destroy its negotiable character or quality, for the instrument on its face still expresses an absolute promise or obligation to pay according to its terms. The condition attached to the indorsement affects only the question as to when payment is to be made.

8. *Liability of indorser*.—Unless he indorses with-

out recourse, as explained above, each indorser, by merely placing his name upon the instrument, warrants that the instrument is genuine and in all respects what it purports to be, that he has good title to it and that all prior parties had capacity to contract. He can be held liable for a breach of these warranties by any subsequent holder of the instrument.

In addition the indorser, by the mere fact of indorsement, agrees that the instrument is at the time of his indorsement valid and enforceable; he agrees that it shall be accepted or paid, or both, according to its terms and that, if it be dishonored and the necessary proceedings on dishonor be duly taken, he will pay the amount thereof to the holder or to any subsequent indorser who may be compelled to pay it.

It will be noticed that the indorser of a promissory note enters into a different contract from that of the maker of the note. The maker agrees to pay in accordance with the terms expressed upon the face of the note. The terms of his contract are, therefore, embodied in the note itself. The terms of the indorser's contract, however, do not appear upon the face of the note or elsewhere. With the exception of the provisions previously discussed in connection with the kinds of indorsement, the terms of the indorser's liability are implied by law.

9. *Liability of accommodation indorser.*—Any person who places his signature upon an instrument,

otherwise than as maker of a promissory note, or drawer or acceptor of a bill of exchange, is deemed to be an indorser and becomes liable upon the instrument as such, unless he clearly indicates by appropriate words written upon the instrument his intention to be bound in some other capacity. Where a person, not otherwise a party to an instrument, places his signature upon it in blank before delivery, he is liable as an indorser in accordance with the following rules:

(a) If the instrument is payable to the order of a third person he is liable to the payee and to all subsequent parties.

(b) If the instrument is payable to the order of the maker or drawer or to bearer, he is liable to all parties subsequent to the maker or drawer.

(c) If he signs for the accommodation of the payee, he is liable to all parties subsequent to the payee.

A party who has signed an instrument either as maker, drawer, acceptor or indorser without receiving value therefor and for the purpose of lending his money to some other person, is called an *accommodation party* and becomes liable on the instrument in the capacity in which he has signed to a holder for value, irrespective of the fact that such holder, at the time of taking the instrument, knew him to be an accommodation party.

Thus if John Doe desires to buy goods from John Sharp upon his note, and if William Brown should indorse the note before its delivery to John Sharp for the purpose of inducing Sharp to extend credit

to Doe, Brown would be described as an *accommodation indorser* and would be liable to pay Sharp provided that Doe failed to pay the note upon its presentment and Sharp immediately gave Brown notice of the default.

Sometimes, however, Brown indorses the note in order to enable the payee, Sharp, to discount the note. In that event Brown is then said to indorse for the accommodation of Sharp and makes himself liable to all holders of the note subsequent to Sharp, but, of course, he is not liable to Sharp.

Again, suppose that John Doe desires to borrow money from the bank but has no security to offer the bank. Brown, being in good credit and willing to assist Doe might make and deliver to Doe his own note for \$10,000 payable to the order of Doe in ninety days, which note Doe could indorse and deliver to the bank and thus procure the loan. In such case Brown is an *accommodation party*. Both Brown and Doe are liable to the bank on the note, but since Brown received no value and gave the note only for the accommodation of Doe, the latter could not hold Brown liable upon the note at maturity.

10. *Other provisions as to indorsement.*—Where an instrument is payable to the order of two or more persons, all of the payees must indorse the instrument in order to pass title unless they are partners. In that case any one of them may make the indorsement.

Of course one person may authorize another to in-

dorse for him and so several payees may authorize one of their number to indorse for all. Since the title of the subsequent holder, in all cases of instruments made payable to order, rests upon the indorsement, it is necessary that the indorser should indorse his name and the names of any other payees for whom he is authorized to indorse in the exact form in which the names appear in the body of the instrument.

If the payee's name has been misspelled or he has been described by the wrong name or by his initials only, he should indorse the instrument in exact accordance with the name as it appears on the face of the instrument and underneath it add his proper signature. Thus if a bill or note intended for John Parsons is made payable to "Jack Parsons," it should be indorsed by him by signing his name "Jack Parsons" immediately followed by his own signature, "John Parsons."

Instruments are frequently made payable to "John Doe, Executor," or "John Doe, Treasurer of the Sphinx Company," or "John Doe, Cashier of the First National Bank." In such cases, if John Doe indorses the instrument, he must indorse it in the same representative capacity. Therefore, his indorsement should read, "John Doe as Executor of William Doe deceased," or "John Doe as Treasurer of the Sphinx Company." A person so indorsing in his representative capacity nevertheless becomes personally liable as well as liable in his representative capacity. Hence, if John Doe as executor wishes

to so indorse as to avoid personal liability and render only the estate of William Doe liable, he should add to his indorsement such words as "without recourse to me individually."

Bills or notes payable to the order of a person as cashier or fiscal officer of a bank or corporation form an exception to the above rule in that such instruments are deemed payable to the corporation instead of the individual. Hence title to the instrument is in the bank or corporation and the instrument may be negotiated by the indorsement of either the individual signing in his representative capacity or the corporation itself indorsing in its own name.

Until it is proven otherwise, every indorsement is presumed to have been added to an instrument before the instrument fell due and at the place indicated in the date of the instrument. The indorsers become liable to each other in the order in which they have indorsed, i. e., each one may hold all preceding indorsers liable upon the instrument and is in turn liable to all subsequent holders.

11. *Necessity of presentment for payment.*—We have seen that the indorser of a promissory note makes no absolute and unqualified promise to pay the note. His promise is contingent not only upon non-payment by the maker but also upon the strict performance by the holder of the instrument of certain conditions. These are that the holder must, on the day that the instrument falls due, present it to the person originally liable thereon and demand payment;

and if payment is not immediately forthcoming, the holder must then give the indorser immediate notice of the dishonor of the instrument. Should the holder consent to any delay in payment or to any change of the terms of the instrument, the effect is to relieve absolutely all prior indorsers from their liability.

12. *What constitutes sufficient presentment.*—When the instrument is payable on a specified date, it must be presented for payment on the day it falls due. When it is payable on demand, it must be presented within a reasonable time after its issue, or in the case of a bill of exchange, within a reasonable time after it reaches the hands of the holder making the presentment. It must be presented by the holder or by some person authorized to receive payment on his behalf, at a reasonable hour on a business day and it must be presented to the person who is primarily liable on the instrument, in other words to the maker of a promissory note or to the acceptor of a bill of exchange. If the person so liable is absent or inaccessible, the presentment may be made to any person found at the place of presentment.

If the instrument specifies a place of payment, for example, the Monroe National Bank, it must be presented at the bank. If no place of payment is specified in the instrument but the address of the person to make payment is given in the instrument, presentment should be made at that address. If the person to make payment does not specify any place of payment or give his address, the instrument may

be presented at his usual place of business or at his residence.

Where the place of business or place of residence cannot be found, the holder must make diligent inquiry and effort to ascertain the residence or place of business within the state or to find the person to make payment and present the instrument to him personally. The holder is not obliged to go outside of the state in which the instrument is payable in order to find the debtor. Reasonable diligence on the part of the holder is all that the law requires in any case.

A sufficient presentment requires that the instrument be actually exhibited to the person who is to make payment, accompanied by a demand for payment. Of course, this presentment may be made to an agent of the person primarily liable, if the agent is authorized to make or refuse payment on behalf of his principal.

When an instrument is made payable at a bank, it is equivalent to an order to the bank to pay the sum for the account of the person making the instrument so payable. Therefore, if the note or bill is payable at a bank, presentment to any employe of the bank at the bank during business hours in the manner in which checks are usually presented for payment is sufficient. In fact if the maker had no funds there to meet the instrument at any time during the day, presentment after business hours but before the bank is closed for the day would be sufficient.

When the note is made by partners, presentment to one partner is sufficient, but if it is made by several persons not partners, presentment must be made to them all, unless a place of payment is specified in the note.

When the principal debtor of the instrument is dead, presentment may still be made at the place of payment, if one is specified in the instrument. If no such place is specified for payment, the instrument must be presented to the executor or administrator of the deceased, if with reasonable diligence he can be found.

If a day of payment falls upon a Sunday or holiday, the instrument is payable on the next succeeding business day. In New York, Saturday is a half holiday. Instruments falling due on Saturday are to be presented for payment on the next succeeding business day, but if payable on demand, the holder has an option of demanding payment on Saturday before twelve o'clock noon.

13. *Notice of dishonor.*—When a negotiable note has been dishonored, as when the maker of a promissory note does not pay it on the day it is due, or the drawee of a bill of exchange fails to accept it when presented for acceptance, or to pay it when presented for payment, notice of dishonor must be given to the drawer of the bill of exchange and to each indorser of a promissory note or of a bill of exchange. A drawer or indorser to whom such notice is not given is dis-

charged unless the circumstances were such as to excuse notice in accordance with the rules which will be stated. The notice may be given:

- (a) By the holder or his agent
- (b) On behalf of any party to the instrument who might be compelled to pay the holder and who would then have the right to reimbursement from the prior indorser or the maker.

Notice of dishonor is frequently given by a notary public or other agent who has been employed to present instruments for payment. In such a case, the agent or notary acts on behalf of all parties to the note subsequent to the person who is primarily liable thereon, and may give notice of dishonor on behalf of all such parties regardless of whether or not he has been specially authorized to do so. But since the holder may receive adequate satisfaction himself and may not be interested in preserving the rights of the prior parties to the instrument, every such party has the right to inform himself as to the payment or non-payment of the instrument and give the notice to persons from or thru whom he received the instrument. In consequence, the notice, altho customarily given in writing, may be given orally and no defect in such notice will invalidate it unless the defect has actually misled the person to whom the notice is given.

When previous indorsers are partners, notice to one of them is sufficient, but if joint parties are not

partners, notice must be given to each one. When any party is dead, notice must be given to his administrator or executor, if one can be found; if there be none, notice may be sent to the last residence or place of business of the deceased. These requirements are very similar to the requirements for presentment for payment.

14. *Within what time must notice of dishonor be given?*—When the person giving and the person receiving notice reside in the same place notice of dishonor must be given at one of three places within the following limits of time:

(a) At the place of business of the person to receive the notice before the close of business hours on the day following the dishonor

(b) At the residence of the person to receive notice before the usual hours of rest on the day following the dishonor

(c) By depositing it in the post-office in time to reach the person to receive notice on the day following the dishonor.

If the parties reside in different places, the notice may be given by mail by depositing it in the post-office in time to go by mail the day following the day of dishonor or by the next mail. If the notice is not sent by mail, it must be given within the time during which a notice given as stated above would have been received in usual course.

Where a notice of dishonor has been duly addressed and deposited in the post-office within the time al-

lowed, the sender is deemed to have given due notice notwithstanding any loss or delay in the mails; the notice may be deposited in any branch post-office or letter box with the same effect.

Where an intermediate indorser receives a notice of dishonor, he has, after the receipt of such notice, the same time for giving notice of dishonor to former parties and may give the notice in the same way. In general, the notice of dishonor must be addressed to a party at the address given by him upon the instrument. If he has given no such address, the notice should be addressed to his customary post-office address. If he lives in one place and has a place of business in another the notice may be sent to either place. If he is known to be sojourning in another place, the notice may be addressed to him there.

15. *Protest*.—The protest is a formal certificate executed by a notary or other agent certifying that a bill or note described therein has been presented for acceptance or presented for payment, as the case may be, and that acceptance or payment has been refused. The instrument must set forth details as to time and place and names of parties. This certificate, when properly executed, is useful as evidence in an action upon such an instrument to prove the dishonor. But protest is legally necessary in the case of only one class of instruments, foreign bills of exchange, i. e., bills of exchange in which the drawer and drawee reside in different states or countries. Protests by notaries are recognized the world over, and when it is intended

to protest a bill or note a notary should be employed to make presentment if one can be found.

REVIEW

State the liability incurred by the maker of a promissory note.

Explain the effect of indorsement in general and the following special forms, blank, special, restrictive, accommodation.

Give the rule for indorsing a note made payable to a person in a representative capacity, so as to avoid incurring personal liability.

Explain why presentment for payment is necessary and what constitutes a sufficient presentment.

State when, how, by whom, and to whom notice of dishonor must be given.

Discuss the circumstances which would excuse notice of dishonor.

Define "protest," and explain when it is necessary.

CHAPTER X

BILLS OF EXCHANGE

1. *Nature*.—The bill of exchange is better known to business men in the United States as a draft. The form of the bill of exchange has already been given. Instead of promising to pay another a certain sum as the maker does in case of a promissory note, the drawer of a bill of exchange signs an unconditional order in writing addressed to another person requiring that person to pay either on demand or at a fixed or determinable future time, a definite sum of money. The payment may be directed to be made either to the person who draws the bill or to some third person. Like a promissory note, if it is made payable to a person or corporation by name merely, it is not negotiable, but if it is made payable *to the order of* such a person or corporation or *to bearer*, it is negotiable.

If both drawer and drawee reside in the same state, the instrument is called an “inland” or “domestic” bill of exchange, but if, as already indicated, the drawer and drawee reside in different states or countries, it is called a “foreign bill.”

When the drawee of a bill of exchange is a bank, the instrument is more commonly described as a check. In fact checks are sometimes described as

bills of exchange drawn on a bank or banker and payable on demand. When a depositor draws a check, he directs his bank to pay the amount specified to the holder of the check on demand. If instead of directing the bank to pay on demand, he should direct the bank to pay "30 days after date" or "10 days after sight," the instrument would still be a bill of exchange but it would not be a check. If the drawee is directed to pay "at sight" or "on presentation" or "on call" or if he is simply directed to pay, no time of payment being expressed, the instrument is payable on demand, i. e., whenever within a reasonable time the holder sees fit to present it and demand payment.

A bill may be addressed to two or more drawees jointly, but since the order must be unconditional, it cannot direct one drawee to pay in the event that another drawee does not pay. The requisites of a promissory note as to certainty of amount and time of payment, as to payment in money and as to absolute terms of the promise which we have discussed above, are as applicable to negotiable bills of exchange as they are to negotiable promissory notes.

2. *Liability of drawee.*—It is the usual practice to address a bill to a drawee with whom the maker has money on deposit, or who is indebted to the maker, or to one who holds money as an agent or trustee for the benefit of the maker. But it does not operate as an assignment of any funds in the hands of the drawee, nor is the drawee liable in any way upon the bill un-

less he accepts it. An accepted bill is best known to business men as an acceptance.

After the bill is presented to the drawee he is allowed twenty-four hours in which to decide whether he will accept or not. His acceptance must be in writing and should be upon the bill itself, but if he destroys it or fails to return it within the time allowed, he is deemed to have accepted it. To say that he accepts the bill is to say that he will pay the amount in accordance with the terms of the bill.

Of course, unless the drawee has previously agreed to accept the bill, he is under no obligation to accept it at all. That being the case he may give a qualified acceptance, he may alter the time or place of payment or make payment conditional upon the happening of some particular event, or he may accept as to a part only of the amount named in the bill. But once having accepted the bill, he is obliged to pay the holder in accordance with the terms of his acceptance. His liability is then like that of the maker of a promissory note. On the other hand the holder of the bill may refuse to take a qualified acceptance and if he does not obtain an unqualified acceptance, he may treat the bill as dishonored by non-acceptance.

3. *Liability of drawer.*—The drawer of the instrument undertakes that on due presentment to the drawee the bill will be accepted and paid according to its terms and also agrees that, if it be dishonored by non-acceptance or non-payment and due notice is

given him of the dishonor, he will himself pay the amount thereof to the holder or to any subsequent indorser who may be compelled to pay it. His liability, like that of an indorser, is conditional upon prompt action by the holder of the bill and it therefore behooves the holder of a bill or check to be alert for his own protection. He must see to it that the instrument is duly presented to the drawee for acceptance or for payment or both and, if it is dishonored by refusal of the drawee either to accept or to pay, the holder must see that due notice is given to the drawer in accordance with the rules previously stated.

Two presentments, one for acceptance and one for payment, may become necessary. For example, take the case where a bill of exchange is made payable 30 days after sight. The holder must present the bill to the drawee for acceptance. If the bill is not accepted, it is dishonored; but if the drawee accepts it, it must be again presented, this time for payment, 30 days after acceptance.

Before the bill has been presented for acceptance, the drawer, by its delivery to the payee, warrants to the payee that there is an existing drawee who will accept or pay the bill according to its terms. Therefore, if it turns out that the drawee is non-existing or cannot be found with due diligence, or when found is incompetent by reason of infancy or imprisonment, or being an alien enemy, presentment of the bill is ex-

cused and the drawer becomes liable upon the instrument exactly as if he had been the maker of a promissory note.

But if the drawee were a competent person and, by refusing to accept, violated his agreement with the drawer, the drawer can in turn recover from the drawee the principal sum and interest and also any damages suffered by the drawer, which may include protest fees and even damages to the drawer's credit. The liability of the drawer thus is seen to be very similar to the liability of an indorser, which has already been considered.

4. *Rights of holder of a negotiable instrument.*—The first right of the holder of a negotiable instrument is to demand payment and if necessary to sue for it in his own name. Payment to him in due course discharges the instrument. Holders are divided into two classes: holders in due course, more commonly spoken of as bona fide holders, and persons who are not holders in due course.

If at the time the holder acquired the instrument it was complete and regular upon its face and not yet due, if at the time he had no knowledge of its having been previously dishonored and took the instrument in good faith without notice of any defect in the instrument or in the title of the person transferring it to him and if he gave value therefor, the owner is a holder in due course. The word *value* as used above means a valuable consideration such as would be sufficient in the case of a contract.'

The reader should note, however, that unlike the case of an ordinary contract, an antecedent indebtedness is a good consideration for a bill or note. For example, Brown is indebted to Sharp for goods purchased with no definite understanding as to the term of credit; such amount is payable on demand. Suppose Brown holds a note of Green's due 30 days hence for \$5,000 which he indorses and delivers to Sharp on account. If Sharp receives the note without notice of any defect, it implies an extension of time to Brown or at least a forbearance on the part of Sharp to sue Brown. The law regards such extension or forbearance as having value; hence Sharp has given value for the note, and is therefore, a holder for value. Suppose that when the note falls due Sharp accepts from Green a renewal of the note, again Sharp has parted with the same valuable right and is therefore the holder of the new note for value.

Suppose in another case that Brown is desirous of purchasing goods from Sharp who insists upon payment and security in advance. Brown who has Green's note in his possession transfers it to Sharp as payment in advance or security for the goods to be delivered in successive lots. If Sharp accepts the note and delivers the first instalment of the goods, amounting to \$500, in ignorance of any defect in Brown's title to the note but is informed of a defect in Brown's title before he delivers the second lot of goods, Sharp will be considered a holder in due course to the extent of the first lot of goods delivered, but

not as to the goods delivered subsequent to his discovery.

A person may be prevented from becoming a holder in due course either by actual notice, i. e., knowledge of some defect or irregularity, or by constructive notice. The holder will not be allowed to say that he was ignorant of some fact which ordinary inspection of the instrument would disclose. The purchaser is charged with notice of whatever facts appear upon the face or back of the instrument received by him. Suspicion of some irregularity or defect which the holder neglects or refuses to investigate is treated as actual knowledge of the defect, since the law does not encourage purchasers to close their eyes to possible defects but rather demands vigilance and good faith. The test applied by law is "knowledge of such facts, i. e., action in taking the instrument amounting to bad faith." If the facts known to him should lead him to inquire and by inquiry he would discover the real situation, he acts in bad faith and the law will withhold from him the protection that it would extend to a holder in due course.

5. *Defenses.*—A fact or set of facts which will defeat an action for the payment of a negotiable instrument is called a defense. Defenses in turn are divided into two classes, *real* defenses and *personal* defenses. A real defense is one which is good against a holder in due course while a personal defense is one which is founded upon the agreement or conduct of the particular person who seeks to enforce the instru-

ment and is good only against him and those who have taken the title from him with notice of such agreement or conduct. Hence a personal defense is not available against a holder in due course. Real defenses include incapacity, illegality, usury and forgery and these must now be considered.

6. *Incapacity*.—Since a minor cannot bind himself, except for the reasonable value of necessities, no minor can be held liable upon a bill or note even by a holder in due course; as to the minor the instrument is void if the minor wishes to take advantage of the defense. However, if Green were a minor and should give his note to Brown, and Brown should indorse the note to Sharp who would take it for value in ignorance of Green's incapacity, Sharp could not compel Green to pay the note even after Green became of full age. But since Brown by indorsing the note warranted that it was genuine and valid and that the maker of the note, Green, had capacity to make the contract embodied in the note, Sharp could recover from Brown upon Brown's liability as indorser, regardless of the fact that the note would be void as against Green.

On the other hand, by special provision of the Negotiable Instrument Law, if a minor acquires a bill or note and indorses or assigns the instrument to another, the new holder acquires title to the instrument and can enforce it against all parties to the instrument except the minor. The same is true in regard to a corporation indorser in the case where the

corporation has not the power to become a party to a negotiable instrument, as is usually the case, for example, with religious corporations.

Incapacity caused by insanity or extreme intoxication destroying mental capacity are defenses to the same extent as infancy. They are good defenses when set up by the lunatic or drunkard, or by their guardian or committee, even against the holder in due course, but no other party to the instrument could take advantage of such a defense.

7. *Illegality*.—The law never requires any one to do an unlawful act nor will it punish him for refusing to perform such an act. Neither will the law assist any one to collect compensation for doing an unlawful thing. Accordingly, when statutes provide that contracts with reference to the doing of a certain thing shall be void, no bill or note given in payment for doing such unlawful act or which provides in itself an obligation to do such forbidden act, can be enforced against any one.

On the other hand, it would be against the interests of the community to make it necessary for each person taking a bill or note in the course of business, to risk the loss of the amount involved because it might appear that preceding parties to the instrument had made unlawful use of it. Therefore, unless the statute of the state in which the bill or note is executed expressly provides that such an instrument shall be *absolutely void*, the instrument will be enforced in the hands of subsequent holders in due course.

Suppose the note were given to pay a gambling debt. The payee, of course, could not enforce it against the maker in any state, but if the payee should indorse it to a holder in due course, such holder could enforce it against either the maker or the indorser unless the statute of that state expressly provided that notes arising from gambling transactions should be absolutely void. In this case, and only this, the defense that the instrument was given for a gambling consideration would be a real defense.

8. *Usury*.—Statutes in many states make usury a real defense. Usury consists of intentionally taking or contracting for a higher rate of interest upon a loan than is allowed by law. New York is one of the states making an usurious contract utterly void and unenforceable even in the hands of a holder in due course. No matter what ingenious arrangement the parties have made, if the court decides that the purpose was to secure an illegal rate of interest for money loaned, neither the principal nor the interest can be recovered from any party to the instrument. Usury laws in most states are less drastic and should be consulted in each case.

It should be noted also that to make usury good as a defense, the instrument must be usurious in its inception, i.e., the bargain which led to the making of the note or bill must have been usurious. But if the instrument were free from such taint as between the original parties to it, the mere transfer or discount of the instrument for more than legal interest is not

usurious and the holder may recover the full amount of the instrument from any of the prior parties thereto.

A contrary rule would amount to holding that while the owner of any other property could sell it in the market for what it would bring, the holder of a promissory note or bill of exchange could not sell it for less than its face value less the legal rate of interest to its maturity, regardless of the credit of the parties to the instrument or of the holder's need of funds. By virtue of the banking statutes in many states, call loans or time loans in excess of certain amounts are not subject to the defense of usury and where the holder in due course of negotiable paper is a bank, usury is not a defense even tho present at the inception of the instrument. Here again it is necessary to consult the statutes in each state.

9. *Forgery*.—The placing of a signature upon a negotiable instrument without authority of the person whose signature it purports to be, or counterfeiting or altering or erasing a genuine negotiable instrument or any part of it with intention to defraud, followed by the delivery of the instrument, is forgery. Forgery confers no rights upon any person as against the person whose name is signed without authority or whose promise is altered without his authority. But the person whose name is forged or whose note is altered must repudiate the forgery as soon as he discovers it and must act fairly and in good faith to all others in regard to the instrument. Just as a prin-

cipal, by acquiescing in the acts of an agent assuming to act for him without authority, is held to have ratified the unauthorized act, so a person whose name is forged may adopt and affirm the forgery as his own act or as having been done with his authority and thus bind himself upon the forged instrument.

If a party receives a bill or note which has been forged and in ignorance of the forgery indorses the instrument to another, by doing so he warrants to the latter that the instrument is genuine. In such case altho the instrument would be worthless in the hands of the first party yet he is liable to his indorsee. Since by his indorsement he has warranted the instrument to be genuine, he will not be permitted to assert later that the instrument is not genuine, especially when such change of position on his part would cause loss to the person dealing with him. This is an illustration of the so-called legal rule of estoppel. Another illustration is where an instrument is shown to a supposed maker or indorser and he is asked if his signature is genuine and, instead of denying, he so acts as to mislead the holder to the latter's damage. In this event he would be held liable on the instrument by estoppel.

In many cases the forgery is not discovered until after the instrument has been paid. In such case the party who has paid the money upon the forged instrument may generally recover the money from the person to whom he has paid it. This is an illustration of the rule that one who pays money to an-

other by mistake may recover it upon discovery of the mistake, unless the person paying was negligent and the person receiving the money was unaware of the mistake and has so changed his position that a recovery by the person who paid would throw the loss unfairly upon his shoulders.

Another case to be noted is where the drawee pays the bill to a holder in due course. In every case where a bill is presented to a drawee for its acceptance or for payment, the drawee is assumed to know the drawer's signature, and if he accepts or pays the instrument he thereby treats the drawer's signature as genuine and in effect warrants it to be so. Therefore, he cannot recover the sum paid, but is left to whatever remedy he may have against the forger. Perhaps the commonest illustration of this rule is a case where a bank pays a check upon the forged name of its depositor. If the forger himself presented the check to the bank, the bank might recover from the forger, but if the check is paid by the bank to a holder in due course, the bank can recover neither from the depositor, for it was not his act, nor from the person receiving payment, for he has been deceived by the bank's assumption that the signature was genuine.

10. *Personal defenses.*—The so-called personal defenses, i. e., those which are not good against a holder in due course, do not invalidate the instrument. They only render it unenforceable against the particular person whose conduct or agreement has given rise to the defense. For example, a bill or note whose

execution or indorsement was obtained by fraud cannot be enforced by the fraudulent party against the party defrauded; but, if the fraudulent party transfers the instrument to a holder in due course, the latter can enforce it against the party defrauded. The reason for this rule is that when in the case of two parties, both innocent of wrong, one must suffer for the fraud of another, the loss ought to fall upon the one who enabled the third party to commit the fraud.

There is a limited class of cases to which the above rules do not apply. Suppose a blind man, thinking he is signing a letter, is defrauded into signing a promissory note; such an instrument is not really his act. The blind man never intended to sign such an instrument at all and logically, therefore, the instrument ought not to be enforced against him. But for the purpose of promoting the freedom of commerce and the free circulation of these convenient instruments of credit, the Negotiable Instruments Law provides that, even in such a case, the note would be enforceable in the hands of a holder in due course.

11. *Lack of consideration.*—We have seen that in all cases of the making or indorsing of negotiable instruments it is presumed that the act was done for a consideration and, therefore, the fact that the instrument was either given or indorsed without consideration does not affect its validity, except between the two parties immediately concerned in that particular transfer of the instrument. Consequently if Brown gives a note to Sharp and Sharp indorses it

to Smith who in turn indorses it to Green, the fact that Sharp gave Brown no value for the note, while it would prevent Sharp from enforcing the note against Brown, would not prevent either Smith or Green from enforcing it against either Sharp or Brown. To allow such a defense to be set up successfully would seriously impair the security and therefore the convenience and value of such mediums of exchange to the community.

12. *Payment.*—As has been said above, a person liable to pay any negotiable instrument is entitled upon payment to have the instrument surrendered to him for cancelation or destruction. Of course it is expected that such an instrument will be paid when due. Consequently any person to whom an overdue bill or note is offered is put upon his inquiry by the very terms of the instrument. Since the date of payment must be disclosed by the terms of the instrument, the law will not permit any one to say that he received the instrument without notice that it was overdue. Negotiable paper is not intended to circulate after it is past due. In other words, upon the day that it falls due, it loses its negotiable character and thereafter has only the legal effect of an ordinary contract. Consequently there can be no such thing as a holder in due course or purchaser for value without notice of an overdue bill or note.

Payment of a bill or note on, or after the day it is due, operates in law as an extinguishment of the instrument, but as there is no presumption that com-

mercial paper will be paid before its maturity payment before maturity does not extinguish the instrument. A holder in due course of an instrument not yet due, by its terms, is not required to make inquiry as to whether or not the instrument has been paid. Consequently the fact that it has been paid before maturity is no defense to the claim of a holder in due course.

A further defense which may become available to persons secondarily liable upon negotiable instruments, i. e., the drawer of a bill of exchange or the indorsers of a bill or note, is that if the holder extends the time of the maker of a note or acceptor of a bill of exchange in which to pay the instrument beyond the date fixed by its terms, the drawer and indorsers are relieved from liability upon the instrument. As we have seen above, the liability of these parties is strictly conditional and contingent; they have the right to insist upon strict performance of the conditions by all subsequent holders.

The foregoing enumeration of defenses, while including the most important and usual, of course, is not complete. Any fact which would be a defense to a contract would be also good as a personal defense to an action upon a negotiable instrument.

REVIEW

Explain the nature and use of a bill of exchange and the difference between a check and other bills of exchange.

Define the liability that a bill of exchange imposes upon a drawer; define an acceptance.

State the liability of the drawer of a bill of exchange before it is accepted; after it has been accepted.

Distinguish a mere "holder" of an instrument from a "holder in due course."

Name several "real defenses" to negotiable instruments and state their legal effect; name several "personal defenses" and explain why they are so called.

CHAPTER XI

CHECKS AND OTHER INSTRUMENTS

1. *Nature of a check.*—A check is a sight draft drawn on a bank. Of all the negotiable instruments, a check is probably the most familiar to the ordinary man. It is essential to a check that its amount be payable on demand. If the instrument is payable on a day subsequent to its date, it is not a check but a bill of exchange. The Uniform Negotiable Instruments Law provides that the rules applicable to a bill of exchange payable on demand are applicable to a check with the exception of the provisions as to presentment, acceptance and assignment.

In common with other bills of exchange, a check must contain an order to pay on demand a definite sum of money; it may or may not contain words of negotiability; but it must be presented to the bank for payment. A check may be indorsed in the same way as other bills of exchange; and it is not an assignment of the money of the depositor in the hands of the bank.

The principal points in which a check differs from other bills of exchange are that a check is always drawn on a bank or banker; it is always payable on demand; it must be drawn on funds actually in the

bank; the death of the drawer of a check revokes it and renders it worthless even in the hands of a holder in due course, while death of a party has no such effect on a bill. A check is in a sense always overdue and hence a person who takes it subsequent to its date is not charged with notice that the check may have been paid or dishonored as in the case of a bill of exchange. Moreover, the drawer of a check, unlike the drawer of a bill of exchange, is not relieved from liability because of delay in presenting the check for payment, unless he can show that he has been damaged by the delay. Some of these points will be considered in more detail.

2. *Relation between bank and depositor.*—Between a bank and a depositor there is a contractual relation and the contract may or may not give to the depositor the privilege of checking; but where the ordinary so-called checking account is opened with a bank the relation established between the bank and the depositor is that of debtor and creditor. The ordinary man, after having made a so-called deposit, thinks and says that he has money in the bank, but this is not the view of the situation taken by the law. There is no money in the bank belonging to the depositor. In the eyes of the law the bank is merely a debtor to the depositor to the amount of his deposit and is under agreement to pay this amount or any part of it on demand. In the case of a checking account the bank is assumed to have agreed further to repay either to the depositor, when he shall so order,

or to any other person upon the depositor's order and in accordance with settled commercial customs.

If, instead of depositing money with the bank, the customer deposits checks, the transaction usually amounts to the bank purchasing the check from the depositor and immediately crediting the depositor's account with the amount. The bank then becomes the owner and holder of the check and the depositor becomes liable only upon his indorsement. But sometimes the bank receives the check only "for collection" in which event the bank does not credit the depositor's account until the proceeds of the check have been actually received. Meantime it receives and collects the check solely as the depositor's agent and at the depositor's risk.

3. *Rights and liability of the drawer of a check.*—As appears above, if the depositor has funds in the bank sufficient to meet the check at the time it is presented for payment, he has the right to expect the bank to pay the check and if the bank fails to pay, the depositor, like the drawer of any other bill of exchange, can recover any damages caused him by the bank's refusal. This includes damages for injury to the depositor's credit if the dishonor of the check causes an impairment of his credit. Of course the bank is not required to make partial payment of a check and will be justified in dishonoring the check if there are not sufficient funds to meet it in full.

Until the bank has either paid or certified the check, the drawer may "stop the check," i. e., give the bank

notice not to pay it. The death of the depositor before certification or payment of the check also revokes the check, even in the hands of a holder in due course. In consequence, if the bank without notice of the depositor's death pays the check even to a holder in due course, the bank cannot charge the amount to the estate of the deceased depositor. The bank, however, could recover the money from the person to whom it had paid the check, as money paid by mistake.

If a drawer draws a check upon a bank without having funds there sufficient to meet it, he is guilty of a fraud and in some states the statute makes such an act a crime. In the state of New York, for example, the law is as follows: "Where such check, draft, or order has been protested, the notice of protest thereof shall be admissible as proof of such presentation, non-payment and protest, and shall be presumptive evidence that there was a lack of funds in or credit with such banks or other depositories."

The drawer does not, by simply drawing and delivering a check, thereby assign any part of the money on deposit to the payee of the check, nor does the delivery of a check in payment of a bill pay or discharge the indebtedness until the check is actually paid by the bank. Apparently the drawer of a check which has been dishonored at the bank comes under no additional liability to the payee of the check because of its dishonor, but if the check has been indorsed by the payee to a holder in due course, the drawer is

liable to such holder in case he stops the check, or in case of its dishonor. As was said before, an unreasonable delay in presenting the check does not relieve the drawer of liability upon the check unless the bank has become insolvent during the interval.

If the bank pays a check to the wrong party, the bank must bear the loss unless the mistake was contributed to by the negligence of the drawer. An example of this is where one negligently allows an incomplete check to get into circulation where the check is subsequently wrongfully filled in and reaches the hands of a holder in due course. The bank alone must bear the loss if it pays a raised or altered check; but the bank may recover its loss from the drawer if the drawer so carelessly made out the check as to facilitate the fraud, such as by leaving blanks unfilled or leaving a space before or after the words or figures specifying the amount, in such manner that alteration could be easily made.

It is, therefore, requisite for the drawer of a check to use the greatest care to leave no unfilled blanks, to see that the check is clearly legible and free from any erasures or alterations, and that his signatures to his checks are uniform and in exact accordance with the signature which he has submitted to the bank as a guide. What has been said about forgery of other negotiable paper and concerning the leaving of blanks therein applies equally to checks.

4. *Rights and liabilities of holder of a check.*—The payee of a check has no legal rights whatever against

the bank. If, however, before presenting a check for certification or payment, the payee indorses the check and delivers it, he makes a new contract in respect to the check, namely, that of an indorser and becomes liable to subsequent holders of the check like any other indorser of a negotiable instrument. While subsequent holders can enforce the payee's liability as an indorser, they have no action against the holder or against the bank until after the check is presented for certification or payment. In order to hold an indorser liable a check must be presented for payment within a reasonable time after its issue and, if it is dishonored, notice must be given to the drawer within the same time which is allowed for notice after the dishonor of a promissory note or a bill of exchange.

However, if there are indorsers upon a check subsequent to the payee of the check, but prior to the present holder, much greater diligence is necessary to preserve the holder's rights against prior indorsers than to preserve his rights against the maker. Whether a check has been presented for payment within a reasonable time, depends upon the circumstances peculiar to each case and no definite time limit can be laid down. These circumstances include distance, the course of mails and the accepted usages of the trade or community. If instead of presenting the check to the bank on which it is drawn the holder deposits it in his own bank, the latter assumes the obligation to present it for payment within a reason-

able time and if the bank neglects to fulfill this duty and the fund which is on deposit to meet the check is lost, the loss falls on the bank rather than upon the depositor.

Sometimes after a check has been drawn but before it has been presented to the bank for certification or payment, an attachment or execution is levied upon the funds of the depositor in the bank. In such a case the attachment creditor secures a prior right to that of the holder of the check. This results from the rule that until the check is presented to the bank it does not operate as an assignment of the depositor's funds in the hands of the bank. The bank still owes the money to the depositor and the debt can be attached.

When the holder has lost a negotiable instrument he, nevertheless, may generally enforce the instrument upon making due proof of its existence and terms. But for the protection of the person liable on the instrument, the holder of the lost instrument is usually required to give a bond to the effect that he will indemnify the person paying the amount against any loss which he may suffer by reason of being compelled to pay the instrument should it subsequently turn up in the hands of a holder in due course.

5. *Certified checks*.—Where a check is presented to the bank on which it is drawn, the holder may demand payment from the bank or ask that the check be certified. Certification by the bank is equivalent

to an acceptance. The balance of the drawer is deemed to be reduced immediately by the amount of the check and said amount is held by the bank to the credit of the holder of the certified check. Certification of the check, therefore, operates as an assignment to the holder of the check of the specified amount of the depositor's funds then in the bank.

The advantage to the holder of a check in having it certified is that thereafter the bank is substituted in place of the drawer and indorsers as debtor to the holder of the check for the amount involved. The drawer and indorsers are thereby discharged, but the credit of the bank is usually much higher than the credit of the drawer and indorsers. A further advantage is that the obligation of the bank, unlike that of the drawer and indorsers, will not be discharged by any delay in presentment, short of the time prescribed in the Statute of Limitations.

It is a common practice for the drawer of the check to have it certified by the bank before he delivers it to the payee. While the check still remains in the hands of the drawer after certification, the relations between himself and the bank remain practically unchanged. The obligation of the bank to the payee and subsequent holders begins with the transfer of the check by the drawer. As in the case of the acceptance of an ordinary bill of exchange, the bank, by certifying a check, warrants to all subsequent holders that the drawer is in existence, that the

check bears his genuine signature and that he had capacity and authority to draw the check.

Moreover, where the bank certifies a check in the hands of a holder subsequent to the payee, it warrants also that the payee is in existence and had capacity to indorse the check. The bank in consequence becomes liable to a holder in due course even tho it turns out that the depositor had no funds to meet the check or that the drawer's name is forged, or that the payee is fictitious, or that there has been fraud in filling blanks or in altering the check *prior* to the certification, but *after* certification its liability to a holder in due course cannot be increased by alteration or altered by a subsequent forged indorsement. But the holder in due course may enforce the note against the bank according to its terms as they stood before the forgery or alteration. Of course negligence on the part of the bank which affords an opportunity for fraudulent alteration of the check exposes it to the same liability for its negligence as obtains with the drawer of the check.

6. *Bill of lading*.—A few instruments having some of the qualities of negotiable instruments should be noticed.

A bill of lading is an instrument issued by the carrier to the consignor of goods. It consists of a receipt for the goods and an agreement to carry them to their destination. It embodies the contract of carriage and the consignor is conclusively presumed

to have read it and agreed to it except in the cases of fraud or mistake. This instrument is considered in detail in the chapter on carriers. We are now concerned only with its negotiability.

The bill of lading is something more than a contract for the shipment of goods. To some extent it actually represents the goods; so that a transfer of the bill amounts to a transfer of the goods themselves. The carrier assumes a liability similar to the acceptor of a bill of exchange. The carrier warrants the quantity of the goods unless he incorporates in the bill words distinctly indicating the contrary, and the purchaser who in good faith gives value for the bill of lading can enforce it against the company according to its terms, regardless of the quantity actually received by the carrier.

In New York and some other states, if the agent of the carrier issues a bill of lading fraudulently or by mistake, altho no goods whatever have been delivered to the carrier, the latter is held bound to a holder in due course by the representation made in the bill by its agent acting within the apparent scope of his authority. It will not be permitted to show as against such a holder of the bill that no goods were actually received. The United States Supreme Court, however, takes the contrary view and holds that the receipt of *some* goods by the carrier is necessary to the validity of the bill.

7. *Coupons*.—Interest coupons are contracts usually in the form of a promissory note, payable to

bearer upon a specified date. Until they are detached from the bond they form a part of the contract contained in the bond and are subject to all the conditions contained in the bond. But the coupons are so made as to be easily detachable from the bond and when detached they have the legal effect of separate negotiable promissory notes. In determining whether or not a given coupon is negotiable, however, if it refers to the bond from which it was detached, it is necessary to examine the bond in order to determine whether or not it contains any provisions restricting the negotiability of the coupons.

In the absence of such restrictions, if the coupons are payable to bearer they pass by delivery like other negotiable instruments and when they reach the hands of a holder in due course they cannot be defeated by personal defenses. The holder of a coupon may ordinarily bring suit upon it in his own name, regardless of whether he is the holder of the bond from which the coupon was detached.

8. *Certificate of deposit*.—A certificate of deposit is a written acknowledgment, issued by a bank, showing that the holder has deposited money in the bank payable on demand, on or after a specified date, to the depositor or his order or to a third person. Such certificates are transferable by indorsement and must be surrendered upon payment of the deposit. In most of the states they are given the same effect by law as a promissory note made by the bank.

9. *Letter of credit*.—A letter of credit is a written

instrument, addressed by one person to another, requesting the latter to give credit to the person in whose favor it is drawn. The drawer promises expressly or by implication that he will repay or guarantee the amount so advanced. It may be addressed by one merchant to another or, as is the more usual case, by one bank to another. The letter itself is ordinarily not negotiable; rather it amounts to an agreement by the issuing bank that it will honor drafts made upon it by the person to whom the letter is addressed up to the amount stated in the letter of credit.

10. *Money orders*.—Money orders are usually bills of exchange issued by post offices or express companies for the transfer of money. They are directed to another post office or to another agency or branch of the express company. They are negotiable, but when issued by a post office in the United States their negotiability is expressly limited to a single transfer, bank transfer excepted.

11. *Stock certificates*.—The nature of a stock certificate is fully set forth in the Modern Business Text on "Corporation Finance." By their terms such certificates are almost invariably made transferable only upon the books of the company, but a custom has grown up by which a blank assignment is printed upon the back of each stock certificate; the holder signs this assignment, leaving the name of the transferee and the date of the transfer blank. This is called an indorsement in blank. A transfer

by the owner of a certificate so indorsed in blank has the legal effect of making the transferee the owner of the stock and gives him the right to compel the corporation to complete the transfer by entering his name upon their books as a stockholder and issuing to him a new certificate. Until the certificate so indorsed in blank is surrendered to the company for cancelation it may pass from hand to hand by mere delivery and possesses practically all of the qualities of negotiability, altho it is not fully recognized by law as a negotiable instrument.

If Brown should borrow \$5,000 from Sharp and deliver to him, as collateral security for the loan, a certificate for 100 shares of stock indorsed in blank and Sharp should in turn borrow \$10,000 from Smith, and deliver Brown's certificate to Smith as collateral security for the \$10,000 loan, Smith, if he were ignorant of Brown's ownership of the certificate, would acquire a right in the certificate superior to Brown's. Brown could recover the certificate from Smith only by paying off the \$10,000 loan. The courts reach this decision by reasoning that, since either Brown or Smith, both innocent of any wrong, must bear the loss caused by Sharp's wrongful act, the loss ought to fall upon Brown, because, by delivering to Sharp the certificate of stock, indorsed in blank, he clothed Sharp with an appearance of ownership, thus giving Sharp an opportunity to deceive. Since stock certificates are transferable by indorsement, and, when so indorsed, pass from hand to

hand like negotiable instruments, and since the holder in due course may acquire rights in them superior to those of the true owner, they come, as a practical matter, very close to being negotiable instruments.

12. *Trade acceptances*.—When a draft or bill of exchange has been drawn by the seller of goods upon the purchaser of the goods and accepted by such purchaser, the instrument is known as a “trade acceptance.” It has the legal effect of any negotiable bill of exchange which has been accepted. It has the additional value of being recognized by the federal reserve banks as commercial paper which is acceptable by them for rediscount or purchase.

13. *Warehouse receipts*.—A warehouseman is one who is engaged in the storage of goods for others for profit. His written receipt in which he acknowledges that he holds certain described goods in storage for the person named in the receipt is called a warehouse receipt. Unless there is a statute to the contrary, a warehouse receipt is not negotiable. Transfer of the receipt does not, as in the case of the transfer of a bill of lading, transfer the title to the goods mentioned nor does the warehouseman, by his receipt, guarantee the quantity of the goods nor that the person placing the goods in the warehouse had good title to them. In some states a warehouse receipt is made negotiable by statute. In such states the receipt is transferable by indorsement and such transfer carries with it title to the goods and a transfer to a holder in due course frees it from personal

defenses but not from the defense that the original depositor of the goods in the warehouse had no title to them. Every taker of a warehouse receipt assumes that risk.

REVIEW

State the legal effect of an ordinary deposit in a bank "for collection."

State the rights and liabilities of (a) the drawer of a check; (b) the bank on which the check is drawn; (c) a bank with which a check on another bank is deposited.

Outline the rights and duties of the holder of a check.

Explain the act of "certification" of a check and its legal effect upon (a) the relation of the bank to the holder of the check; (b) the relation of the bank to the drawer.

Explain the nature and use of each of the following instruments and state what negotiable qualities each possesses: bill of lading; bond coupon; certificate of deposit; money order; stock certificate; trade acceptance; warehouse receipt.

CHAPTER XII

SALES—STATUTE OF FRAUDS

1. *Principal aspects of the law of sales.*—In this chapter we shall discuss the nature of contracts for the sale of personal property, both executed and executory, as distinguished from other contracts, and the form of such contracts under the Statute of Frauds and the Uniform Sales Act. Following this we shall treat of the performance of contracts of sale and of the rights and obligations of the parties thereunder, including conditions and warranties.

2. *Provisions of the statute.*—The English Sale of Goods Act, section 4, expresses the effect of the Statute of Frauds with some change of language. It has been followed, with some modifications, in the Uniform Sales Act which has been adopted in New York, New Jersey, Connecticut, Massachusetts, Rhode Island, Pennsylvania, Michigan, Illinois, Wisconsin, Iowa, Oregon and several other states. Substantially the same provisions with some changes are contained in the Statute of Frauds as enacted in most of the other states. Section 4 of the Uniform Sales Act provides as follows:

(1) A contract to sell or a sale of any goods or choses in action of the value of five hundred dollars or upwards shall not be enforceable by action unless the buyer shall

accept part of the goods or choses in action so contracted to be sold or sold, and actually receive the same or give something in earnest to bind the contract, or in part payment, or unless some note or memorandum in writing of the contract or sale be signed by the party to be charged or his agent in that behalf.

(2) The provisions of this section apply to every such contract or sale, notwithstanding that the goods may be intended to be delivered at some future time, or may not at the time of such contract or sale be actually made, procured, or provided, or fit or ready for delivery, or some act may be requisite for the making or completing thereof, or rendering the same fit for delivery; but if the goods are to be manufactured by the seller especially for the buyer and are not suitable for sale to others in the ordinary course of the seller's business, the provisions of this section shall not apply.

(3) There is an acceptance of goods within the meaning of this section when the buyer, either before or after delivery of the goods, expresses by words or conduct his assent to becoming the owner of those specific goods.

3. Sales and executory contracts to sell.—A sale involves the immediate transfer of title to the chattel from vendor to vendee. A contract to sell is a contract to transfer title at a later time, as on delivery and payment. When the subject-matter of the sale is ascertained, the terms of the sale agreed upon, and nothing remains to be done except to deliver the goods and pay and receive the price, the transaction is held to be a sale, title passing at once to the vendee, who assumes from that moment the risk of loss incident to ownership. This question will be more fully discussed in the following chapter on performance of contracts of sales.

The Statute applies to both types of transactions, sales and contracts to sell. All doubts arising under the Statute of Frauds are removed by the precise phraseology of the Uniform Sales Act. Conditional sales or contracts to sell are also covered by the Statute.

4. *Contracts to sell distinguished from contracts for work and labor.*—In England it is held that if the contract is to result in the transfer of title to a chattel for a price, irrespective of whether the chattel was to be manufactured by the vendor or not, either at the special order of the purchaser so as to be valuable to him alone, or in the regular course of the vendor's business, it is a sale under the Statute.

The Uniform Sales Act follows on this point the rule as laid down first in Massachusetts and followed in possibly a majority of the other states, that the Statute does not apply if the chattel is manufactured on special order, so that it is not manufactured in the regular course of the maker's business, and is designed especially for the purchaser and is therefore not suitable for sale in the regular course of the business of the maker.

In New York a different rule prevailed previous to 1911, when the Uniform Sales Act was adopted, to the effect that the Statute did not apply where the chattel was not in existence at the time of the making of the contract, but did apply if the chattel was in existence, tho some work had to be done on it

before it was ready for delivery. This was followed in many states, some of which have not adopted the Uniform Sales Act.

5. *What is included within "sales of goods."*—Rights or choses in action were held in England not to be included under the old Statute. In the United States it has been generally held that choses in action having a visible and tangible form and commonly dealt with and transferred as property, including shares of stock, bonds, mortgages, bills and notes, come under the old Statutes. All choses in action are included by express terms in the Uniform Sales Act. A "chose in action" is simply a right of action to recover money or property capable of assignment under the law.

Growing annual crops, water, ice, manure and fixtures annexed by a tenant for years are each and all personal property for the purpose of sale as distinct things separate and apart from the land. This is true tho they pass with the land as part of it when the land is transferred without their reservation. Therefore, a sale or contract to sell any of these things comes under the Statute as a sale of goods and chattels.

In the case of the owner of the land who sells fixtures, trees or buildings to be removed by the purchaser, if title is to pass at once, the contract falls under the provision of the Statute of Frauds relating to sales of interests in land; if an executory con-

tract to sell after severance is made in express terms, the sale is a sale of goods, and the section of the Statute we are discussing applies.

6. *Provision as to value of the goods.*—The English Statute of Frauds provided that the minimum value of the goods sold to bring the transaction within the Statute should be £10, and the amount of \$50 or more was generally fixed by the statutes of the different states, tho a few have modified somewhat this provision. New York and several of the other states which have adopted the Uniform Sales Act have retained the old amount of \$50 in this connection instead of adopting the figure \$500, which the Uniform Sales Act provides. Successive, distinct purchases of different articles are regarded as separate and distinct contracts in applying this provision of the Statute. However, in any such case, if only one contract was made, tho several items are included, the sum total of the amount fixed must be taken in determining whether the Statute applies or not.

7. *Acceptance and receipt of part of the goods.*—Receipt usually precedes acceptance, but acceptance may come first. Acceptance is established by any acts of ownership such as a sale, mortgaging, storing or transporting of the goods by the buyer as owner. Such receipt and acceptance, tho long after the making of the contract, makes the transaction good without a writing. The danger of fraud is greatly reduced when the transaction is evidenced in this way by overt acts. Receipt means merely the

taking of possession by the buyer, and whether or not such possession has passed, either to the buyer personally or to a third party as his bailee with his assent, is a question of fact. There can be no doubt that possession passes, if the parties so intend, without a physical handing over of the property, it appearing that the seller relinquishes control and the buyer assumes it.

In New York, however, it is held that there must be some physical assumption of possession other than mere words in order that a receipt and acceptance under the Statute will be found to exist. Delivery to a common carrier is a receipt but not an acceptance even if the carrier has been designated by the purchaser. However, if the purchaser has passed on or selected the goods before shipment, delivery to the carrier takes the transaction out of the Statute, since such delivery amounts to receipt by the purchaser.

The transfer of a bill of lading or warehouse receipt to the purchaser will amount to a receipt if the right to control, and therefore possession, passes to him.

8. *Part payment under the statute.*—The usual case of payment of part of the purchase price presents no difficulty, and the Statute is satisfied. Since exchanges or barters come within the Statute, part payment may be the delivery of all or part of the goods which were to be given in exchange. Notes and checks are usually construed as conditional payment only until actually paid, and they will not

satisfy the Statute unless it is clear that they were given and accepted in absolute payment. The time of payment may be at any time after the contract is made as well as at that precise time. In a few states the Statute provides that payment must be at the time the contract is made.

9. *The memorandum in writing.*—The note or memorandum of the sale may be made at any time prior to the starting of an action on the contract, even before the contract is made. It may be in any form, as in letters, telegrams, deeds, wills or the like. It must give the names of the parties and the terms of the sale or contract to sell.

It has been a point of greatest controversy as to whether the consideration must be described. The prevailing rule is that a consideration which has been performed need not be referred to, but an executory consideration in a bilateral contract must state the consideration because performance of it is a condition of the promise to sell, and therefore must be stated in any accurate written description of the vendor's promise.

In executed sales where the price has been paid no memorandum is necessary because of the payment of the price, but in executory contracts to sell in which payment or tender of the price is a condition of the promise to sell, the memorandum does not describe the contract or promise of the vendor unless the price is stated. If no fixed price is agreed upon no reference to price need appear in the memoran-

dum, as the law implies the reasonable value in such cases. The property must also be described, and any additional terms, such as warranties, must appear in the memorandum. The memorandum, moreover, must be signed by the party to be charged, namely by the defendant who is being sued on the contract, or by his duly authorized agent.

REVIEW

Outline the provisions of section 4 of the Uniform Sales Act.

Define what choses in action are included within "sales of goods."

Explain the provisions as to the value of goods sold to bring the transaction within the Statute of Frauds and its modification in states which have adopted the Uniform Sales Act.

Discuss acceptance and receipt of part of the goods with regard to legal possession.

Give the prevailing rule with respect to the mentioning of consideration (a) when it has been performed and (b) in executory contracts.

CHAPTER XIII

SALE—PERFORMANCE—RIGHTS AND LIABILITIES OF PARTIES

1. *Delivery and payment of the price.*—The primary duties of the buyer and seller under a sale or a contract to sell is for the seller to deliver the goods and the buyer to receive and pay for them as the contract provides. In the absence of express provision in the contract to the contrary, such delivery and payment are concurrent conditions, that is, each must be ready, willing and able, the one to deliver the goods on payment of the price, the other to pay the price on delivery. All this is set forth in precise terms in sections 41 and 42 of the Uniform Sales Act, and is declaratory of the well-established principles of contract explained in the chapter on performance of contracts.

2. *Time and place of delivery.*—Section 43 of the Uniform Sales Act provides as to the place of delivery as follows:

(1) Whether it is for the buyer to take possession of the goods or for the seller to send them to the buyer, is a question of fact depending in each case on the contract, express or implied, between the parties. Apart from any such contract, express or implied, or usage of trade to the contrary, the place of delivery is the seller's place of busi-

ness, if he has one, and if not, his residence, but in case of a contract to sell or a sale of specific goods, which to the knowledge of the parties when the contract or the sale was made were in some other place, then that place is the place of delivery.

(2) When by a contract to sell or a sale the seller is bound to send the goods to the buyer, but no time for sending them is fixed, the seller is bound to send them within a reasonable time.

(3) Where the goods at the time of the sale are in the possession of a third person, the seller has not fulfilled his obligation to deliver to the buyer unless and until such third person acknowledges to the buyer that he holds the goods on the buyer's behalf; but as against all others than the seller the buyer shall be regarded as having received delivery from the time when such third person first has notice of the sale. Nothing in this section, however, shall affect the operation of the issue or transfer of any document of title to goods.

(4) Demand or tender of delivery may be treated as ineffectual unless made at a reasonable hour. What is a reasonable hour is a question of fact.

(5) Unless otherwise agreed, the expenses of and incidental to putting the goods into a deliverable state must be borne by the seller.

The above section is simply declaratory of the accepted law as to the details of delivery, as it existed prior to the Statute, and as it exists generally to-day not only in the many states which have adopted the Uniform Sales Law, but also in the other states that have not. The section sums the matter up so admirably that further elaboration is unnecessary.

3. *Delivery to a common carrier.*—When by the contract the seller is to send the goods to the buyer,

delivery to the buyer is made by delivery to a common carrier for the purpose of shipment to the buyer. This is the case whether the buyer has specified the carrier or whether he has been selected by the seller. If a contrary intent appears, as where the carrier is directed to deliver on the seller's order, or if the seller undertakes to make actual delivery to the buyer, or at a particular place, or undertakes to pay the freight to the buyer or to a particular place, title does not pass and delivery is not made until the goods have been actually delivered to the buyer or reached the place agreed upon.

In shipping the goods the seller must protect the buyer by a contract on his behalf which shall be reasonable under the circumstances; if he fails to do so, such delivery to the carrier may be treated by the buyer as no delivery, or he may accept the goods and hold the seller for damages.

If the case is one where it is usual to insure the goods in transit and the seller knew or should have known this, the seller must give the buyer notice of the shipment in time to permit the buyer to insure the goods. If he fails to give this notice the goods are at his risk during transit.

These rules are set forth in precise terms in Section 46 of the Uniform Sales Act.

4. *Delivery of a greater or less quantity.*—If more goods are delivered than the contract calls for the buyer may reject them all, or retain only those contracted for. If he keeps them all he must pay for

them at the contract rate. If less goods are delivered than the contract calls for the buyer may reject them; but if he accepts them knowing that the seller does not intend to deliver the rest he must pay for them at the contract rate; if he does not know this he is liable only for their fair market value.

If goods, not included in the contract, are delivered mixed with goods covered by the contract, the buyer may reject all or accept those which he had contracted to purchase, rejecting the rest. Section 44 of the Uniform Sales Act sets forth the above provisions.

All the foregoing provisions of the Statute are subject to any special agreement of the parties or custom of trade in modification of them; they are all simply declaratory of the principles of the law of sales established as prevailing law by the courts.

5. *Examination of the goods by the buyer.*—Section 47 of the Uniform Sales Act provides that when goods are delivered to the buyer which he has not examined, no acceptance takes place until he has a reasonable opportunity to examine them. On tendering the goods the seller must give the buyer a reasonable opportunity to examine them, but when no delivery is to be made by the carrier thru whom the goods are shipped to the buyer until the price is paid, there is no right of inspection until after the price is paid, since the contract requires payment before delivery. If, later, the goods are found to be inferior, the buyer may reject them and recover his

money. However, the seller has no right to ship goods on such conditions unless the contract's express terms or a custom of the trade permits it. In such case the buyer may reject the goods.

6. *Transfer of title.*—If the goods are definitely set aside or ascertained, and in a deliverable state, title passes at once, tho the time of payment or delivery or both are to take place later. But if the seller is to do anything to the goods to put them in a state for delivery, title does not pass until this has been done.

In delivery of the goods on a contract of "sale and return," the intention being to transfer title at once, with an option in the buyer to return the goods instead of paying for them, title passes at once but reverts to the seller when the buyer returns or tenders back the goods to the seller within the time fixed in the contract, or within a reasonable time when no time is so fixed.

Delivery on approval transfers title only on express acceptance by word or act, or by the buyer retaining the goods beyond the time fixed for him to return them, or beyond a reasonable time if no such time is fixed.

Goods to be selected or manufactured in the future pass to the buyer only at the moment when the goods have been ascertained and have been applied to the contract with the mutual assent of both parties expressed by word or inferred from their conduct; and

delivery of the goods to the buyer or to a carrier for the buyer is presumably an appropriation of such goods to the contract so that the title passes.

If the contract of sale requires delivery to the buyer, or delivery at a specified place, or that the seller pay cost of transportation to the buyer or to a specified place, title does not pass until the goods have been delivered to the buyer or have reached the place agreed upon. These rules are laid down in section 19 of the Uniform Sales Act. They express the law as it generally prevails in the States which have not adopted the Uniform Sales Act as well as in these where it is law.

7. *Goods shipped C. O. D.*—Goods shipped “cash on delivery” pass to the buyer when delivered to the carrier, according to weight of authority, tho the contrary has been held in several states. This provision is given effect by construing it as giving a retention of possession with a lien for the price, title passing as in other cases of delivery to a carrier.

8. *Reservation of title or possession by sellers.*—Express provisions of this nature in the contract of sale will, of course, be given full effect when the goods are delivered to a carrier. A provision in the bill of lading that the goods be delivered to the seller or his agent is construed as preventing transfer of titles, but only for the purpose of securing performance by the buyer of his obligations under the contract.

The same result follows if the bill of lading is retained in the possession of the seller, tho it calls for delivery to the buyer.

9. *Risk of loss.*—Generally the risk of loss accompanies the legal title or property right in the goods, remaining in the seller until title passes to the buyer, but passing to the buyer with the title when it is transferred to him. But this may be changed in any way the parties please by express agreement. When delivery is made to the buyer, and title has been retained by way of securing performance by the buyer of his contract including cases of conditional sales, the goods are at the buyer's risk from the time of delivery to him or to the carrier for him. If delivery is delayed by fault of either party, the risk of loss is with the party so in fault if the loss is one which might not have occurred had delivery been made. Section 22 of the Uniform Sales Act contains these provisions which express the prevailing law.

10. *Goods shipped under bill of lading.*—In the case of goods shipped under a bill of lading, as in other cases, the risk of loss accompanies the legal title. If the goods are not shipped as ordered, title, of course, does not pass and the risk of loss is not with the consignee. If properly shipped, title and risk of loss pass to the buyer. The retention of title, by way of security, does not prevent the risk from passing to the buyer, as appears from the preceding section.

11. *Sale by person not having title to goods sold.*—The general rule is that a sale of goods made by a person without title is absolutely void, and in no way affects the true owner's right to recover the goods. The Factor's Acts of the different states have modified this rule in cases of goods left in the possession of a factor in his own name, and sales made by him under common law rule bind the owner, if made to a purchaser for value without notice, even tho sold by the factor in violation of the owner's instructions since there is a holding out of the factor as having general authority to sell. The Factor's Acts have extended this doctrine to the pledging of such goods by a factor, so that the owner cannot recover the goods until the loan to the factor which the goods secure has been paid. This is discussed in the chapter on the law of agency.

12. *Conditional sales.*—In the case of conditional sale, title is reserved in the seller as security for the payment of the purchase price, the possession passing to the buyer. The danger of fraud in these cases has led to the enactment of statutes in nearly all the states making such sales void, as to subsequent innocent purchasers or encumbrances for value if not filed or recorded in ways provided by the Statute, so that subsequent purchasers or encumbrancers of the property may have notice thereof.

If the contract of conditional sale is not filed as the Statute requires—and the same Statute includes also chattel mortgages—the contract of conditional sale

or chattel mortgage cannot be set up to defeat the title of any person buying or taking as security such property from the conditional vendee or chattel mortgagor for value and without notice of the chattel mortgage or contract of conditional sale. By statute, therefore, title passes to such purchasers, tho the vendor did not have the true title to transfer. The risk of loss in these cases of conditional sale is with the buyer, as the legal title is reserved by the seller only as security for payment of the purchase price.

13. *Sale with retention of possession by seller.*—Section 25 of the Uniform Sales Act provides as follows:

Where a person having sold goods continues in possession of the goods, or of negotiable documents of title to the goods, the delivery or transfer by that person, or by an agent acting for him, of the goods or documents of title under any sale, pledge, or other disposition thereof, to any person receiving and paying value for the same in good faith and without notice of the previous sale, shall have the same effect as if the person making the delivery or transfer were expressly authorized by the owner of the goods to make the same.

This is, of course, the law in those states which have adopted the Uniform Sales Act; yet it also expresses the prevailing law in the other states, tho the decisions and statutory provisions of many of the states vary considerably, and are confused with the effect of such retention upon the rights of creditors. The discussion of these variations in detail of the law in

such states is, obviously, outside the scope of this text.

14. *Express warranties in sales.*—Section 12 of the Uniform Sales Act defines express warranty as follows:

Any affirmation of fact or any promise by the seller relating to the goods is an express warranty if the natural tendency of such affirmation or promise is to induce the buyer to purchase the goods, and if the buyer purchases the goods relying thereon. No affirmation of the value of the goods, nor any statement purporting to be a statement of the seller's opinion only shall be construed as a warranty.

A warranty, therefore, may be a collateral promise amounting to a contract, or an affirmation of fact, as distinguished from a mere statement of opinion, on which the seller expects the buyer to rely, the law making him liable as for a warranty tho no intent to make a promise expressly appears. Positive statements of fact as to quality are regarded usually as affirmations of fact and therefore warranties.

The distinction between representations and warranties so often made in the cases has caused much confusion, but it is generally true that representations, as distinguished from warranties in the law, are merely expressions of opinion not intended as positive assertions of fact.

15. *Obvious defects—inspection.*—A warranty in general terms, as a matter of interpretation, is held not to include obvious particular defects not specifically referred to in the warranty. This is for the reason that the parties probably did not intend the

warranty to cover such defects which both must have known about. But it has often been said that a warranty against an obvious defect cannot be enforced. Certainly this is not the law where the warranty takes the form of a collateral contract based on mutual assent and consideration.

If the warranty is based on a representation of fact not amounting to an express contract, with a promise implied by law to do justice because of the fraud which otherwise would result in misleading the other party, there is a great deal to support the position that the other party must make some effort to protect himself. Therefore, he should not be protected by the law as against obvious defects which he could have readily discovered by a casual examination.

Where the defect is not obvious, but would be disclosed if a careful examination were made, and the buyer had the right to make the examination, but failed to make it or failed to make it carefully, he is nevertheless protected by the warranty, whichever form it takes. He has the right in cases of express warranty to rely on the seller's warranty, according to the prevailing law.

16. *Implied warranty of title.*—Section 13 of the Uniform Sales Act provides that, in a contract to sell or a sale, unless a contrary intention appears, there is:

(1) An implied warranty on the part of the seller that in case of a sale he has a right to sell the goods, and that

in the case of a contract to sell he will have a right to sell the goods at the time when the property is to pass

(2) An implied warranty that the buyer shall have and enjoy quiet possession of the goods as against any lawful claims existing at the time of the sale

(3) An implied warranty that the goods shall be free at the time of the sale from any charge or encumbrance in favor of any third person, not declared or known to the buyer, before or at the time when the contract or sale is made

(4) This section shall not, however, be held to render liable a sheriff, auctioneer, mortgagee or other person professing to sell by virtue of authority in fact or law goods in which a third person has a legal or equitable interest.

This expresses the law as it generally prevails throughout the United States. Rights of action of all kinds, whether in the form of bonds, negotiable paper, stocks, etc., or mere parol rights of action in contract subject to assignment, are included. Barter is also included. The parties may by express provision exclude a warranty of title, and such exclusion will be implied where both know of the defect and make the contract on that basis.

17. *Implied warranty of quality.*—Section 15 of this same act provides that:

Subject to the provisions of this act and of any statute in that behalf, there is no implied warranty or condition as to the quality or fitness for any particular purpose of goods applied under a contract to sell or a sale, except as follows:

(1) Where the buyer, expressly or by implication, makes known to the seller the particular purpose for which the goods are required, and it appears that the buyer relies

on the seller's skill or judgment (whether he be the grower or manufacturer or not), there is an implied warranty that the goods shall be reasonably fit for such purpose

(2) Where the goods are bought by description from a seller who deals in goods of that description (whether he be the grower or manufacturer or not) there is an implied warranty that the goods shall be of merchantable quality.

If the buyer has examined the goods there is no implied warranty as regards defects which such examination ought to have revealed

(3) In the case of a contract to sell or a sale of a specified article under its patent or other trade name, there is no implied warranty as to its fitness for any particular purpose

(5) An implied warranty or condition as to quality or fitness for a particular purpose may be annexed by the usage of trade

(6) An express warranty or condition does not negative a warranty or condition implied under this act unless inconsistent therewith.

Where the goods are specified the warranty of quality is implied by law rather than from any inferred agreement of the parties, and it will be implied, therefore, only in those cases where justice and fair dealing require it. It must appear that the buyer relied, and had the right to rely, upon the skill or judgment of the seller in buying the goods. This is held to be the case where the seller is the manufacturer of the goods, and therefore is in a position to know all about them. In England and many of the states the same rule applies to sales by a regular dealer in the goods for the same reasons.

Many of the states, however, have refused to ex-

tend the rule to sales by dealers, tho this is now changed in such states as have adopted the Uniform Sales Act. This Act extends the rule to all cases where it appears that reliance was in fact placed upon the skill or judgment of the seller, whether he be dealer or manufacturer or not.

When the goods are bought by description it is a plainly implied term of the contract that only merchantable goods of the specified description are intended and the warranty is therefore based on the true intent of the parties. In both cases it is clear that no such warranty should be implied where the buyer has an opportunity to inspect the goods and a reasonable inspection would disclose their defects.

The warranty that the goods are fit for the purpose for which they are purchased is based on the same principles as the warranty of merchantable quality.

18. *No warranty broken when buyer gets what he contracted for.*—When the contract is for the purchase of a definite thing known to both parties, or is definitely described in the contract, so that it cannot be reasonably inferred that the buyer relied on the seller's special judgment or skill, no warranty is implied. It is a question of fact in each case, turning on whether the parties understood that the seller's special knowledge or skill was being relied on or not.

The seller warrants generally that the goods are merchantable and fit for the general use for which they were intended, but not that they were fit for the

specific use to which the buyer intended to put them. Thus a sale of a specified boiler and 320 feet of radiation carried with it no warranty that it would heat the house of the buyer. It would be different if the seller had estimated what size of boiler and amount of radiation would have been required to heat the house, as the buyer would then have relied on his skill and special knowledge.

19. *Warranty that food sold for immediate consumption by a dealer is fit.*—No warranty that food sold for immediate consumption by a dealer is fit, is included in the general provision of the Uniform Sales Act. Yet in states which have not adopted the Act and in which dealers are not charged with warranty of quality, it is well settled that dealers are bound by warranty that such food is fit for consumption as intended.

20. *Merchantability.*—The term merchantability means only that the goods are readily salable as goods of the quality or grade which they are supposed to be, not that they are of first quality.

21. *Sale by sample.*—An implied warranty arises out of a sale by sample which gives the buyer an action for damages if the bulk of the goods does not correspond with the sample in quality. It implies that the buyer shall have reasonable opportunity to compare the goods with the sample by examination, and that, if the seller is a dealer in the goods, he warrants against defects rendering them unmerchantable

and which would not be apparent on a reasonable examination of the sample.

REVIEW

Outline the provisions of the Uniform Sales Act regarding time and place of delivery.

Explain what alternatives are open to a buyer when the seller delivers goods in greater or less quantity.

Tell when title passes in the case of goods shipped under a bill of lading.

Under the Uniform Sales Act, name the warranties that are implied.

Define merchantability.

CHAPTER XIV

BAILMENTS AND CARRIERS

1. *Nature of a bailment.*—A bailment exists in any case in which goods belonging to one person are held by another with the owner's express or implied consent. It is the duty of the holder or bailee to hold and care for the goods according to his contract, and to return the goods on demand to the owner, called the bailor. The transaction is still a bailment tho work is to be done on the property of the bailor which will alter it in form, such as where cloth is made into clothes, or milk into butter. The duty of the bailee to return the bailor's property, irrespective of its form at the moment, is clear, and therefore, a bailment exists.

2. *When the bailed goods belong to a third person.* The rule, generally laid down, that a bailee cannot deny the bailor's title, means merely that he cannot set up an adverse title in himself. If he discovers that a third person is the owner of the goods, he will be liable for the goods to the owner should he return them to the bailor. This is as true, by weight of authority, of common carriers as it is of other bailees. In cases of this kind the best course for the bailee will be usually to bring the two rival claimants into court to fight out between themselves their conflicting

claims. This may be done by a bill of interpleader in equity,¹ in New York and other states, if an action against the bailee has been started by either claimant.

3. *Gratuitous bailments*.—A bailment to care for goods without compensation to the bailee, or a bailment for the use of the goods by the bailee without compensation to the bailor, is a gratuitous bailment. In either case no contract exists because of the absence of consideration. The duty to use reasonable care in these cases is simply an application of the law of negligence. If the bailee is guilty of a failure to use the care which an average man would use under the circumstances, he is guilty of negligence, and liable for the damages resulting from such wrong or tort.

It is said that a gratuitous bailee in the first class of cases is liable only for gross negligence. This means that he is not held to as high a standard of care as would be necessary if he were receiving pay for holding the goods. It is said that he is liable for slight negligence if he is getting the beneficial use of the particular property for nothing. In other words the bailee is held to a higher degree of care in safeguarding the goods in this latter case than he would be if he were paying for their use.

¹ "Interpleader is a mode of compelling two or more persons, who severally claim the same thing, debt or duty from the party liable therefor, to litigate the title thereto between themselves, the party liable having incurred no independent liability to any of the claimants, and being merely in the position of stake holder, without interest in the matter himself."—"The American and English Encyclopaedia of Law."

Of course in cases of doubt as to whether negligence existed or not, the absence of compensation is a material circumstance which may turn the scale one way or the other. The trouble with the form of statement used by the courts is that it may be and, in the past, often has been misconstrued to mean in the first case that there may be legal negligence without liability, a position that is quite impossible.

4. *Bailments not gratuitous*.—If the bailment is not gratuitous, there is a valid consideration and a contract exists. The ordinary standard of care, reasonable care under the circumstances, applies in these cases. If a bailee in such a case uses the property in a way not authorized by the contract of bailment, and the property is damaged or destroyed, whether because of such authorized use or not, he is liable for the loss. Tho this is called conversion, a term used in law to designate assuming control for one's own use of the property of another, it is not legally conversion unless an intent to convert, in destruction of the property right of the bailor, is made out; this is seldom the case.

The law simply holds the bailee liable for any damage to the property happening during the diversion to unauthorized uses without regard to whether the diversion caused the damage or not. For instance if a man hired a horse to go to town A and he drives the horse beyond town A to town B, the man or bailee becomes absolutely liable if the horse dies during such diversion from the original agreement, tho he died of

some disease with which the driving to town B could have had no connection.

5. *Pledges*.—A pledge is the delivery of personal property to a creditor to secure payment of a debt or performance of any contractual obligation in favor of the creditor, or pledgee. Bonds or other obligations under seal and negotiable instruments may be pledged by transfer of possession. Choses or rights of action represented by documents, such as insurance policies and stock certificates, may be pledged in the same way. Tho other rights of action may be assigned by way of security, such transactions are not pledges because there is no transfer of physical possession.

Payment of the debt, of course, discharges the pledge. Tender of payment, not accepted by the pledgee, also discharges the lien, so that the pledgor may then recover possession of the property pledged. A man cannot retain his security for a debt after rejecting a valid tender of the amount due. Tender is usually made on condition that the pledge be returned, and is valid when so made. The debt may be enforced by action, however, without enforcing the pledge or tendering back the pledged property.

The pledgee may sell the pledged property after default of the debtor, on reasonable notice to him, or by foreclosure of the lien in equity. Statutes regulate the enforcement of pledges in many states. The pledgee's right, apart from statute, is an implied power of sale reasonably incident to the pledge.

Either party may assign or transfer to another his property interest in the thing pledged, subject to the rights of the other party.

6. *Storage or warehouse bailments.*—When property is placed in storage the duty of the owner is to pay the price of storage agreed upon or its reasonable value as the case may be. The duty of a warehouseman is to use reasonable care under the circumstances, and he impliedly represents and warrants that he has the skill of the average person qualified to perform the particular contract of storage involved.

The law of warehousemen has been codified in a uniform statute enacted in a large majority of the states. It provides that warehouse receipts which make the goods deliverable *to order* or *to bearer* are negotiable, and that a provision in such a receipt that it shall be non-negotiable is void. If the receipt is non-negotiable, the act provides that the words “non-negotiable” shall be placed plainly on its face, otherwise, one taking it and believing it to be negotiable, will have the right, at his option, to enforce it as such.

The rights and duties of the parties are provided for in detail by the statute, and apply as in usual cases of bailment as to due care, duty to deliver to the owner, excuses for non-delivery, etc. These necessarily are modified by the provisions making receipts negotiable when payable *to order* or *to bearer*. The act also provides for a warehouseman’s lien for his charges and the enforcement thereof, giving him relief from the common law which does not recognize such a lien.

7. *Bailments with innkeepers.*—An innkeeper, like a common carrier, has been held liable to a special standard of care as a bailee of his guest's personal property. He is one who carries on the business of supplying all persons who apply for a temporary stay with food and lodging and other necessities. An owner of a private house who occasionally accepts paying guests, but rejects others, is not an innkeeper. One who furnishes food without lodging accommodations or lodging without food is not an innkeeper, but on the other hand, a hotel keeper with a restaurant run on the European plan is. He is liable, irrespective of his negligence or wilful wrong, for all loss or damage to his guest's property. This is the law in many states, irrespective of whether the goods were left in his possession by the guest or under his general control by bringing them on the premises. In some states, however, the hotel keeper is not liable for loss by fire or from other causes not due to his fault. His liability for a theft, however, tho committed by a stranger, is generally settled. He may limit his liability by reasonable rules, such as requiring guests to deposit valuables to be kept in his safe. Goods brought on the premises, not as baggage incident to the traveler's accommodation, but to be exhibited for sale or as samples, do not come under this special rule of liability. As to such goods, he is chargeable like the ordinary bailee for reasonable care only.

8. *Liability of common carriers.*—A common car-

rier is one holding himself out as ready to accept anyone's goods for transportation, as distinguished from a carrier who undertakes to act as such only when a special contract to that effect is made. If not a common carrier he incurs the usual liabilities of the simple bailee for hire. If he is a common carrier he is liable as insurer for any damage or destruction of the goods shipped, except when caused by acts of God, acts of public enemies of the State, damage or destruction due to seizure under execution or attachment or other valid legal processes and by damage due to the negligence of the owner himself or to the inherent character of the goods shipped. Fire caused by lightning is an act of God, excusing the carrier, but fire arising in other ways, which might have been foreseen and the loss prevented, does not excuse the carrier from liability. The carrier further is liable for damage from theft, collision, and other causes, tho there is entire absence of negligence on his part.

9. *Acts of God.*—When the damage results directly and solely from natural causes, excluding human agencies, it is an “act of God,” and the carrier is excused. Fires from lightning, storm and tempest, extraordinary frosts, tides, snowstorms, earthquakes, and the like are all considered as acts of God.

10. *Public enemies.*—Public enemies are limited to the forces of a hostile power at war with us, and therefore, pirates, criminals, rioters and the like are not included. In case of rebellion it must have proceeded so far that a *de facto* state of war exists in order that

the rule will apply as between the opposing forces.

11. *Damages due to inherent character of goods shipped.*—When live stock is shipped and damage arises out of the inherent nature of the animals, the carrier is not liable unless negligence is proved. Decay of perishable goods not due to the carrier's negligence is another illustration of this rule.

12. *Carrier's liability for delay.*—A common carrier is not subject to any special liability in case of delay beyond the liability of ordinary carriers. The carrier must exercise due care at all times, and if an emergency arises, the standard of care applying is the general standard, reasonable care under the circumstances to meet the emergency, to deliver the goods and to overcome obstacles that may have arisen.

When delay results from the carrier's fault all the damage resulting to the owner may be recovered, as a fall in the market price of the goods, or damage to the goods themselves, or both.

13. *Limiting liability by express contract.*—Common carriers may limit their liability by express provision in the contract with the shipper only to an extent that is reasonable and not contrary to public policy. Any general stipulation that it shall not be charged with negligence is void as contrary to public policy. Where the contract excepts liability from fire, tempest or other specified causes, the carrier is liable if its own negligence contributed to the loss, whether freedom from liability for such negligence was expressly provided for or not. In New York,

however, it is held that a clause of this kind relieves the carrier, whether or not its negligence contributed to the loss. A few states permit exemptions from ordinary negligence, but not from gross negligence.

14. *Provisions restricting damages to a fixed sum.*

Provisions restricting damages to a fixed sum are valid if made for the purpose of agreeing upon liquidated damages approximating the apparent value of the goods shipped. But, if made arbitrarily without regard to such value, they will be void as to damage resulting from the carrier's negligence. However, a valuation fixed in advance in the absence of some statement by the shipper or knowledge of the carrier to the contrary, will be valid because the shipper will be estopped from denying such valuation on which the carrier received the goods for shipment. Thus goods shipped in closed packages, not open to inspection by the carrier, are subject to this rule as to a valuation fixed by the carrier in the contract of carriage, and limiting its liability accordingly. These matters of limitation of liability by contract differ widely under statutes in different states and also under the United States statutes relating to interstate commerce.

REVIEW

Distinguish between the obligations of a bailee when he is enjoying the use of property for nothing and when he is paying for its use.

Describe the responsibility of warehousemen, innkeepers and common carriers in regard to their positions as bailees.

State what constitutes an "act of God" and what effect such an act has on the carrier's liability.

Tell to what extent a common carrier may limit its liability on a contract with a shipper.

Explain what provisions restricting damages are valid.

CHAPTER XV

AGENCY—CREATION AND TERMINATION

1. *Nature of agency.*—An agent is simply a representative of the principal appointed to act for him. The law of agency is based on the fundamental principle of representation, recognized more or less completely from the early beginnings of English law, that the acts of a duly authorized agent doing what he was authorized to do are the acts of his principal, and bind the principal as tho he had acted in person.

In its broader sense the relation of principal and agent includes that of master and servant, as both relations depend upon this same fundamental doctrine. In legal and commercial usage, however, an agent is a representative employed to act for the principal in the making and negotiating of contracts and other commercial relations, while a servant is one who performs for his master acts of service of all kinds not resulting in contracts. The representative may be both agent and servant in the same transaction, as in the case of a traveling salesman using his principal's car in going about taking orders. In running the car he is his principal's servant, and the principal's liability for his negligent operation of the car will be determined according to the law applying to master and servant, but in the negotiating of sales and the

taking of orders he acts in the capacity of agent. This distinction is a purely formal one, and is held because of the more convenient treatment of the law relating to the matter rather than because of any actual difference in principle.

2. *Agency created by express appointment.*—The relation of principal and agent usually arises by express appointment of the agent by the principal. This appointment as a rule takes the form of a contract, but an enforceable contract is not at all necessary. The giving of express authority by one person to another to act in his behalf creates the relation of principal and agent between the parties, tho the agent's work is to be gratuitous. Whether authority to act as agent in any case has been given is a question of fact to be decided in each case. Of course, where the agent's work is intended to be gratuitous there is no contract between the parties because of lack of consideration; but contracts made with third parties by such agent for his principal within the scope of his authority are valid and enforceable without regard to whether there is a contract between the principal and the agent or not.

3. *Competency of the parties.*—In a previous chapter it was shown that certain persons, infants, insane persons, drunken persons, married women and corporations are subject to certain limitations in their power to make contracts. Such limitations apply as a matter of course to any contracts which they may undertake to perform thru agents.

If any of them on the other hand act as agents, their contracts properly made within the scope of the agency are binding upon the principal. But such contracts as the principal may make with them, for the performance of the agency, are subject to the limitations already discussed.

4. *Unincorporated associations as principals.*—Unincorporated clubs, political parties, college classes, and the like, are not legal persons and therefore cannot be principals. But the members may by their joint act appoint an agent to act for all of them, and if such is the fact, they will be bound by what he does within the scope of his authority. The question is, did the members intend to become bound jointly so that each intended to pledge his personal credit, or did they intend that payment should be made out of the joint funds of the association?

Usually in these cases the members are not held because the intent to pledge their personal credit is generally lacking. However, in cases in which the joint enterprise is directly or indirectly for the individual, financial benefit of the members, they will be held liable. So, also where the constitution and by-laws of the association contain provisions that they shall be bound, the necessary intent to give the agent or officer of the association authority to act as their joint agent will be found to exist.

5. *Joint agents.*—Where two or more persons are appointed as agents to act for a principal they must act together in the performance of their agency. The

principal has a right to rely on the combined discretion and judgment of all of them. Of course, a partnership as an agent acts thru any one of its members, since the act of one partner is the act of the firm, provided it is within the scope of the partnership business.

So also a corporation as an agent will necessarily act thru its board of directors by majority vote. In most instances of incorporated agents the usual transactions of the corporation as agent may be performed thru its executive officers without action by the directors.

6. *Form of appointment, writing and seals.*—At common law, authority to execute an instrument under seal had to be under seal, and therefore in writing. But written authorization of an agent is not necessary in other cases, even where the agency involves the making of written contracts, unless a statute so provides in the particular state when the agency is created. Therefore authority to execute a written contract for the sale of land need not be in writing.

In many states to-day seals have been abolished, and therefore, in these states, parol authority to an agent is always sufficient. In most of the other states it is held that the chance affixing of a seal to an instrument will not invalidate a parol power to the agent to execute it, if the use of the seal was not directed by the principal and was not essential to the validity of the instrument. As the instruments which require a seal, principally conveyances of real estate,

are very few it follows that the old rule finds little practical application. In New York, tho deeds conveying land need not be under seal, the Statute expressly requires that, if such a deed is signed by an agent, his authority must be in writing.

7. *Creation of agency by ratification.*—If a person enters into a contract in behalf of a principal, but without authority or in excess of his authority, the person for whom he acts may ratify his act, thus making it as valid as tho expressly authorized. Most of the law of agency is simply the law of contracts applied to cases involving the principle of representation, but this particular doctrine belongs to agency alone; it cannot be explained on the basis of principles of contract. If it is argued that the transaction is an offer, accepted when the ratification occurs, the theory of contract fails in cases in which performance by the third person has been completed before ratification, for then the consideration for the principal's promise would be past. Yet ratification is as valid in that case as where the contract or promise of the third person is still executory. All that can be said, therefore, is that it is simply a rule of agency having no direct relation to the principles of contract.

8. *Requisites of ratification.*—In order that there may be a ratification there must in the first place be a principal in existence when the contract was made, capable of authorizing the contract. A contract made in behalf of a corporation not yet formed cannot be ratified by the corporation after it comes into ex-

istence. So called "adoption" of a contract by a corporation after it is incorporated is really nothing more than the accepting of an offer which continues by its terms until acted on by the corporation after it is incorporated, the contract then arising and not relating back to the original date as it would in case of ratification.

As a second essential requisite the agent must either affirmatively state that he is acting for a third person as principal or the facts must be such as to show that he was acting in that capacity. If an agent with authority to buy goods at a certain price buys in his own name at a higher price, an attempted ratification fails because the agent made the contract in his own name. There is nothing to show that he was acting for the principal. But where a son makes contracts in his own name to have extensive repairs and improvements made in his mother's property, it is apparent from the facts that he intended to act for his mother, and ratification is good. But pretending to act for the alleged principal is not enough to permit ratification if it is evident that the pretense was false, and made so as to induce the third person to contract with the alleged agent, and that as a matter of actual fact he had no such intent.

The third essential is that the principal must express his intent to ratify with knowledge of all material facts, either in words or by conduct. Express ratification needs no elaboration. Ratification by conduct arises usually thru the acceptance of benefits

under the contract with knowledge of the facts. Any conduct showing an intent to ratify will be enough. Ignorance of a material fact, if established, defeats ratification. A man cannot ratify that of which he is ignorant.

9. *Form of ratification.*—Ratification must be in writing and under seal only in those cases in which a written or sealed authorization would have been necessary if the act had been authorized. We have seen that a seal is necessary only in cases where a sealed instrument is to be executed, and that the use of a seal where it was not necessary and not required by the principal does not invalidate the parol authority which otherwise would be perfectly good. Written authority or ratification is not necessary in the case of contracts in writing not under seal, tho statutes in some states require written authority to execute deeds and leases which have to be in writing, tho not under seal.

10. *Right to withdraw before ratification.*—Before ratification neither the principal nor the third party is in any way bound, and therefore the third party may withdraw or cancel the so-called contract before ratification has taken place.

11. *Effects of ratification.*—The contract becomes thru ratification as effective and valid in all respects as if it had been originally authorized, not only as to principal and third party, but also as to principal and agent. The relating back of the ratification is actually a fiction which the law finds convenient so that

justice may be done, and this fiction is recognized as such where its operation would result in obvious injustice. Therefore where the law requires the giving of a notice of a stated time, as for instance a notice to quit or of dishonor, a notice, invalid because unauthorized, is not validated by ratification so as to take effect as of the original date. It will be a good notice only as of the date of the ratification duly communicated, which would be the first valid notice.

So, also, the rights of third parties, such as attaching creditors, arising after the unauthorized act and before ratification of it, will not be defeated by such ratification. The fiction will be applied as between the parties, but not so as to destroy a right which a stranger to the transaction acquired before ratification. The purchase or other unauthorized act of the agent was really void, and a subsequent attachment or execution upon the goods before ratification gives the stranger an actual lien which cannot be affected by the legal fiction of relating back.

12. *Agency arising by estoppel.*—A man who makes a false statement of a material fact to another by which the second, acting as a reasonable man, is misled, is estopped from denying the truth of his false statement, if asserting the truth would result in damage to the person who was misled by the false statement. A simple illustration of this principle is when, for instance, Smith tells Jones that he has sold his horse to Robinson, and that it can be bought from Robinson at a bargain. Jones buys the horse from

Robinson. The fact is that Smith had merely loaned the horse to Robinson for a week. In an action by Smith against Jones to recover the horse Smith would be estopped from denying the truth of his false statement that he had sold the horse to Robinson. Jones, therefore, would have title to the horse by estoppel because Smith would be estopped from setting up his real title and ownership.

This principle applies to agency in any case where a man falsely holds out another to be his agent to a third person who deals with the alleged agent in the belief that the representation was true. An agency arises by estoppel because the principal will be estopped from denying the truth of his false statement, and he will be held liable for the acts and contracts of the agent with such third person exactly as tho the agency had existed as he said it did.

The misrepresentation may and usually is by conduct rather than by express words. When a man has permitted another to act for him in a series of transactions without dissent, tho admittedly he has never given him authority, an agency by estoppel arises as to the person with whom such transactions occurred. Thus in a case where a clerk was permitted to cash small checks to get money to be used for petty cash without objection, tho admittedly he had not been authorized to indorse checks, the principal was estopped from denying his authority to the bank. The bank had a right to rely upon the apparent authority given to the clerk by this series of transactions,

tho the clerk subsequently had cashed such checks and stolen the money.

13. *Agency to collect on bond and mortgage from possession of the documents.*—If an agent has negotiated a loan for his principal, the lender, or has purchased an existing bond and mortgage for him, and the principal leaves the bond and mortgage in the possession of the agent, tho notifying him that he has no power to accept payment of principal or interest, he will be estopped from denying the agent's authority to accept such payments. The leaving of the papers in the possession of the agent who negotiated the loan in his behalf originally is held by the courts to be an act legally amounting to the holding out of the agent as having power to receive payments of both interest and principal. The mortgagor is protected in making such payments whether he saw the papers or not. However, the fact that he saw the papers on one occasion will not justify him in assuming that the papers are still in the agent's possession later. He will not be protected and must pay over again if the bond and mortgage have passed from the agent's possession, as in the case of a forged assignment by the agent to some stranger.

Nevertheless an agency by estoppel may exist where the possession of the bond and mortgage has not been left with the agent. If the agent has regularly received such payments and turned them over to the principal who has received them without objection, an agency by estoppel arises out of the princi-

pal's conduct as amounting to a holding out of the agent as being authorized to accept further payments.

14. *Termination of relation of principal and agent.* The relation of principal and agent ends by the terms of the contract or appointment creating the agency upon the arriving of the date or the happening of the event on which it was to end according to the contract. It may, of course, be ended by mutual agreement. It may also be ended absolutely at any time by either party without the consent and against the will of the other, tho such termination may involve a breach of contract, if a valid contract existed to continue the agency for a fixed period.

15. *What constitutes revocation.*—No form of express revocation is necessary. A power of attorney under seal may be revoked by parol. All that is necessary is that the principal notify the agent that his power to represent him is ended. Revocation is implied from circumstances showing that the principal intended to revoke. This will necessarily be true when he disposes of the subject-matter or loses control of it; it is true also if it is destroyed by fire, or if the subject-matter is an animal and it dies. Appointment of another agent to do the same act revokes the authority of the first, when the act is one for the performance of which only one of them may be employed. However, in most cases several agents may be employed to accomplish the desired result, so that the appointment of another agent will not revoke an existing agency, as in the sale of a house or the col-

lection of a debt. Tho only one may succeed, several may be employed to try.

16. *Notice of revocation.*—Notice of the revocation to the agent is obviously necessary. Notice to third persons is required only for the purpose of preventing an estoppel in case of a continuing agency which involves a succession of transactions with the same persons who would have a right to believe that the agency still continued unless notice of revocation were given to them.

17. *Revocation by operation of law.*—The general law of contracts, as treated in earlier chapters, deal with the termination of contracts thru operation of law, and these rules apply equally to the contract of agency. Like other contracts, it will be ended by a change in the law which makes performance illegal and therefore impossible. This is illustrated by a contract of employment with an insurance company to sell insurance made illegal and therefore impossible by the taking away of the charter and forced dissolution of the company.

18. *Death of either party terminates the agency.*—A dead man cannot act thru an agent, and therefore his death necessarily terminates any existing agency. The agent's death also necessarily brings his contract to an end. Survival of the power after the principal's death where the power is coupled with an interest in the subject-matter will be discussed hereafter. Bankruptcy also terminates any agency relative to the principal's property or contracts, since

everything of that nature passes to the assignee in bankruptcy.

19. *Irrevocable agencies.*—A power coupled with an interest in the subject-matter cannot be revoked except by mutual consent during the principal's life, nor is it revoked by his death. The usual case is where the property involved is transferred to the agent to secure a debt due him, with power to sell and pay himself the debt out of the proceeds. Here the power to sell runs with his title to the property and is necessary to give effect to the security. As the title is in himself, the difficulty of transferring the title of a dead man as his representative is obviated.

The later cases recognize the fact that exactly the same principle applies when an equitable interest in the subject-matter has been transferred by way of security, tho the legal title has not passed. Therefore an agent to collect rents, with power to apply the rents to the payment of a loan, the loan having been made as part of the contract, was held to survive the death of the principal for whom the rents were collected. Tho the rents had not been assigned, nevertheless in equity they were regarded as mortgaged to secure the debt, and the power to collect them was of the essence of the security.

In these cases no security of the nature of an equitable mortgage arises unless the debt which it secures was incurred in reliance upon the security. When a legal mortgage or pledge exists this element of consideration is not necessary. The transfer of the legal

title or interest by way of security for a past debt, is sufficient. However, if no title or interest is conveyed at law a mere interest in the proceeds of the sale to be made by the agent is not enough. His agency is revoked by the principal's death in all such cases. A power coupled with an obligation is also irrevocable. In these cases the agent has assumed an obligation to a third person relying on his agency. The injustice of canceling the power by which the agent may protect himself in these cases is apparent. Therefore, death of the principal does not take away the agent's power where he has incurred liability to a third person in the discharge of his contract as agent, and, of course, it cannot be revoked by the principal during his life. Thus where the agent promised to pay a sum of money to a third person at the order of the principal from funds of the principal in the agent's hands, the principal could not thereafter revoke his authority to apply the funds to the payment as ordered.

REVIEW

Define agency.

Mention the ways in which agency may arise.

Outline the requisites of ratification.

Explain how agency may arise by estoppel.

State how agency may be terminated.

CHAPTER XVI

PRINCIPAL, AGENT AND THIRD PERSONS

1. *Obligations of principal to agent.*—The agent's right of compensation is determined by the express terms of the contract, subject to the general principles of the law of contracts as explained in preceding chapters. If the services are rendered on request, the law presumes a promise to pay their reasonable value, that is, a promise is implied from the request. Of course if it appears affirmatively that the services are intended to be gratuitous no such promise will be inferred. This is illustrated by cases of services obviously intended to be gratuitous between father and son or other immediate members of the same family, or medical attention between two doctors and their families, or mutual legal services between two lawyers, rendered in each case as a matter of friendship and professional courtesy, or the case of the introduction of a purchaser of real property to the owner by a neighbor when nothing is said about a commission.

Even without a request, the acceptance of services, when there is no good reason to regard them as tendered gratuitously, gives rise to a promise implied in fact to pay their reasonable value.

2. *Real estate brokers' commissions.*—Commissions are not earned by real estate brokers for selling real property or securing loans until they have produced a purchaser ready, willing and able to buy the property on the vendor's terms, or a lender ready, willing and able to make the loan. If a contract of sale is signed the vendor accepts the purchaser as ready, willing and able and the commission is earned. But the broker is not deprived of his commission when the vendor refuses to make a contract after the purchaser is introduced to him who is ready, willing and able to buy on the vendor's terms as given to the agent. So also, if the vendor's title is defective, and the sale falls thru on that account, the broker may recover his commission.

3. *Effect of revocation of agency on compensation.* When the agent or servant is discharged without cause in breach of a contract to employ him for a stated period, he may at once sue for breach of contract and recover the entire damages sustained by him, prospective as well as present. That is, he may recover his full wages or salary under the contract, less such amount as he has been able to earn or should have earned at work of the same general character up to the time of the trial, and less also such sum as he should be able to earn in the future at work of the same general character during the balance of the period for which he was employed. The plaintiff in New York and generally elsewhere simply proves his contract of service and the breach. He then be-

comes entitled to his wages for the entire period following the breach. The defendant may then reduce his recovery by proving what the plaintiff has earned or should have earned, and what he should earn in the future under the above rule. If the servant or agent breaks the contract he may recover wages already earned and payable, less damages for the breach.

If the contract of service is for no definite period it is at the will of either party and may be ended by either without liability for damages. The agent or servant may then recover full wages for the actual period of his service at the rate fixed in the contract. Payment of wages by the week, month or year does not create an obligation to complete the period in these cases. He may recover the *pro rata* part of his wages for the time that he actually worked.

When the contract of service is ended by operation of law, or by death, insanity, illness or other cause without fault of either party, the full wages earned up to that time may be recovered, without the deduction or addition of damages for breach of contract since there has been no breach. In case of the principal's bankruptcy, however, tho the agency is ended, liability for damages arising from the termination of the service exists because the bankruptcy is regarded as a breach of contract.

4. *Discharge of real estate brokers.*—Brokers working on a commission basis are not employed by a contract of employment. Payment depends entirely

on their success in finding a purchaser for the property of their principal. An unilateral contract arises when they have performed their part by introducing a purchaser ready, willing and able to buy on the terms fixed by the owner. The broker is not bound in any way, and therefore the owner is equally free, and may withdraw the property at any time without any payment to the agent even for disbursements. The agent makes such expenditures as for advertising in the hope of securing a commission. There must be a consideration from the broker to the owner to support a promise not to withdraw the property for a stated time, or to give the broker the exclusive agency. Even then the owner may withdraw the property in breach of his contract, but by doing so he incurs liability for damages.

5. *Compensation where agent acts for both sides.*—If an agent acts for both sides with their knowledge he, of course, is entitled to compensation from both. But if he conceals the fact that he is acting for both sides his conduct is a fraud or potential fraud as to each, and he is entitled to receive nothing for his services from either party. If it has been paid, each principal, upon discovering the facts, may recover the amount paid. Such service under the law is worth nothing.

Not only does the agent forfeit all compensation in such cases, but he is also liable for damages in an action brought by each of his principals. The vendor may recover a sum equal to what the agent

was to receive from the purchaser, as the agent could have sold the property to the purchaser for that much more had he been honestly representing the vendor. The purchaser may recover the amount which the agent was to receive from the vendor, since he could have purchased the property for that much less if he had been acting honestly as agent of the purchaser.

It seems settled under the later cases that where the broker is employed merely to bring the parties together so that they may make their own bargain without any effort on his part to get them to arrive at terms, he can recover the agreed commissions from both and, of course, he incurs no liability for damages. This is so where he finds a purchaser ready to pay the price fixed by the vendor without negotiation. It is argued that the vendor gets his price and has nothing to complain of. This is poor law and worse morals, and probably will not last. The broker is bound to get the best price he can for his principal, and if he finds a buyer willing to pay more than what the vendor asks the broker should not be allowed in effect to pocket the excess in the form of a commission from the purchaser.

6. *Illegal services.*—Agents can recover nothing for illegal services, such as lobbying contracts, wagering contracts, including contracts for “futures” in the sale of commodities, and the like. A real estate broker must have a license to act as such in New York, New Jersey, and many other states, or be subject to a penalty for failing to comply with the law.

Furthermore, in such states a broker cannot recover commissions unless he has a license.

On the other hand, servants and agents in minor capacities acting for principals in illegal enterprises are not permitted to steal their employers' money or property. They must account for what comes to them unless they are in effect joint principals in the illegal business. In this event the law gives no remedy as between the illegal participants.

7. *Reimbursement and indemnity*.—The principal must reimburse the agent for all payments made or liabilities reasonably incurred by the agent in the due performance of his duties as agent. This is not true, however, if the enterprise in which the parties were engaged was illegal and the agent knew of the illegality.

The agent is entitled to indemnity from his principal if he has incurred liability to a third party while acting in good faith and according to instructions in his principal's behalf. Thus a railroad conductor, instructed to reject a certain kind of ticket, who was held for damages by a passenger whom he ejected from the train pursuant to such instructions, was held to be entitled to indemnity from the railroad company.

So also an agent who sells goods belonging to a stranger at his principal's direction in the belief that they were the principal's goods, or one who otherwise converts goods of another acting in good faith on his principal's instructions, will be entitled to indemnity

from the principal. If he knows in each case the true facts, so that he is a wilful wrongdoer, he is not entitled to indemnity; the same is true, if the act is illegal and the agent is aware of the illegality. The law leaves joint wrongdoers where it finds them.

8. *Obligations of agent to principal.*—The relation of principal and agent imposes obligations upon the latter which must now be considered.

(a) *Obedience.*—An agent must follow his principal's instructions, and is liable for any damages which result from any material departure from them. Thus where flour was shipped to an agent to sell at once, and the agent delayed the sale for some time because of market conditions and in the hope of getting a higher price, tho he could have readily sold the flour at once at a slight concession from the market price, he was held liable for the loss arising from a considerable drop in the market price. If the agent sends a claim for collection to one person or bank, tho directed by his principal to send it to another, he is liable for any loss that may result. The delay by a certain agent in purchasing tea in China, the agent hoping for a lower price, resulted in charging him with the loss when the price advanced, since it appeared that he could have purchased the tea at the price set by his principal if he had acted with reasonable promptness.

(b) *Duty to use reasonable care and skill.*—An agent must use the care which would be exercised by the average man of his profession or calling. A law-

yer in acting for a client must exercise the skill of the average lawyer; a financial man, in investing money for his client, or lending it on collateral security, must exercise the skill and show the knowledge of investments which one has the right to expect of the average financial man familiar with such affairs. A real estate agent in renting property to tenants must make reasonable investigation as to the solvency of the tenants. An agent to collect debts must use due diligence and employ the usual means of collection. He will be liable for a failure to make presentment and demand for payment, and to give notice of dishonor as required by law in collecting negotiable bills or notes.

In special emergencies where the agent cannot communicate with his principal in time and the literal carrying out of his instructions is impossible, he is permitted to do what seems best in the reasonable exercise of his discretion. Thus an agent in charge of a cargo of merchandise to be sold at a foreign port, finding on arrival that there is no market for the commodity at that port, except at ruinous prices, may seek the nearest market and dispose of the cargo to the best advantage under the circumstances.

(c) *Good faith*.—An agent is a fiduciary and is held to the highest standards of good faith in his relations with his principal. That is why, as has been noted, an agent cannot be permitted to act for both parties without their knowledge. Neither can he act for his own private gain in the performance of his

duties as agent. An agent to buy cannot buy from himself, and on discovering such fact the principal may repudiate the transaction without any proof that the price was unfair. It is for the principal alone to decide whether or not he will ratify the purchase, irrespective of whether he was injured or benefited.

An attorney employed to examine a title cannot acquire an adverse lien or title and enforce it against his principal. An agent in charge of his principal's land who should pay the taxes or advise his principal of their nonpayment, cannot buy the land at a tax sale and set up the tax title against his principal. In such cases the agent would hold the land as trustee for his principal.

As a fiduciary, the agent must keep accurate accounts and render accounts to his principal when required, and turn over to his principal all money or other property belonging to his principal which comes into his hands.

9. *Delegation of authority by agent to others.*—The performance of all kinds of routine duties requiring no particular skill or discretion may be turned over by the agent to clerks or other subordinates. The service upon a tenant of a notice to quit, or the service of the different papers in an action conducted by an attorney for his client, or the typewriting and mailing of letters, etc., and the drawing up and signing of documents as instructed by the agent, are illustrations of what may be delegated. Lawyers as a matter of custom may employ other lawyers in their

offices and may use them under supervision very freely in the performance of important duties to their clients. Generally, however, matters involving the judgment and discretion of the agent cannot be delegated to a third person without the principal's consent. In all these cases the employe of the agent acts as the representative of the agent, who is responsible to the principal for what he does. His acts are the agent's acts, and he is not by himself an agent of the principal, tho the principal is bound by his acts as acts of the agent.

10. *Sub-agents*.—The agent may appoint sub-agents to act as agents of the principal if authority is given him to do this. No difficulty arises in the case of a general manager with authority to employ and discharge subordinates. He is among other things an agent to employ other agents. The difficulty arises in an agency for a particular purpose, as to collect a bill or note, or to bring an action at law. When a bill or note is given to a bank for collection the depositor understands that his bank must send the instrument to another bank if it is payable in another place some distance away. Is the correspondent bank agent of the home bank or of the owner of the paper in such case? The more general rule is that laid down in the New York cases to the effect that the home bank remains liable thruout to the owner of the paper and will be liable for the negligence or other wrong of the correspondent bank. In many states, however, it is held that the home bank discharges its

duty in exercising due care in the selection of the correspondent bank which then becomes agent of the owner to which he must look for damages arising out of its negligence.

11. *Liability of gratuitous agents.*—That gratuitous agents cannot be held liable for breach of contract goes without saying, since no contract exists because of the absence of a consideration. If a gratuitous agent has actually entered upon the performance of his agency, however, and is therefore negligent in the performance of it, he is liable for negligence. It is said in many cases that such an agent, acting gratuitously is called on to exercise “slight” care, or that he is liable only for “gross” negligence. These expressions “slight” and “gross” are meaningless, except as they express the idea that payment of compensation for the service should be considered as one of the circumstances of the case in deciding whether reasonable care had been used or not.

The gratuitous agent must use the skill and knowledge which he pretends to have, either as a lawyer, financial man, real estate expert, or the like. If he has failed to exercise the skill and knowledge of the average man of his profession or calling in the discharge of the agency, he has been guilty of negligence and will be liable accordingly. In a doubtful case of negligence the gratuitous nature of the agency will be material, but not otherwise. Negligence is negligence, and is made no better or worse so far as liability is concerned by calling it “slight” or “gross.”

Where the gratuitous agent has not entered upon the service at all, neglecting or forgetting it, as, for instance, to take out insurance on a ship, he cannot be held. Since he simply has failed to do anything, he cannot be held for doing it negligently. He cannot be held in contract, as we have seen, because of absence of consideration.

12. *Liability of principal to third persons.*—That the principal is liable for contracts or other acts of his agent made or done within the actual or apparent scope of his authority has been emphasized heretofore as a fundamental principle of agency. Difficulties arise in determining whether or not an act of the agent was within the apparent scope of his authority. He has express authority to do everything which is necessary and reasonable in accomplishing what was expressly authorized. When he has not actual authority to do a thing, the principal will, nevertheless, be bound by his acts if he held out the agent expressly or impliedly as having such authority. Cases illustrative of this have been discussed already under the subject of agency by estoppel.

The starting point of the law of the principal's liability to third parties is that the third party dealing with the agent must find out what authority the agent actually has, and if he has not been misled by a false statement or the holding out by the principal, he can hold the principal only for such acts of the agent as come fairly within the scope of his actual authority. It will be helpful to inquire into the na-

ture of the general scope of the agent's authority in the more important classes of agents for illustrations of the general principles by which the scope of an agent's authority may be determined.

13. *General managers or general agents.*—If an agent is made general manager of a business he has actual authority to do anything, or make any contract, coming fairly within the carrying on of the business. Secret instructions by his principal will not alter this. In the case of such instructions not to do things fairly coming within the limits of the business, tho the agent has no actual authority to do these things, there is a holding out of the agent as having such authority because of the nature of the business. Under such circumstances persons dealing with the agent may hold the principal liable for such acts of the agent unless they knew of the secret instructions.

14. *Authority of agents to sell.*—An agency to sell carries with it the power to fix the price and the terms of sale generally, and to receive payment if the agent has possession of the goods. He cannot usually give credit and, therefore, he can only sell for cash, if he has possession. If he has not possession he has no authority to receive payment, unless expressly authorized, unless it is the custom of the trade, or unless he has been permitted to accept payment in similar transactions with the same purchaser.

He has no authority to give a warranty of quality in the usual case. Such authority will exist when expressly given, or if it is the general custom of the trade

to give warranties in sales of such goods, or when in similar sales by the same agent to the same purchaser warranties were given to the knowledge of the principal.

He has no authority to sell on credit unless it is customary in the trade to sell such goods on credit, or unless he has made sales before to the same vendee on credit, ratified by the principal. He has no implied authority to barter, pledge or mortgage the goods, or to sell them at auction.

15. *Authority of agents to buy.*—Agents to buy cannot buy on credit if they have received from the principal the money to pay for the goods. If not, the power to buy on credit is clearly implied.

16. *Factors.*—Factors are men employed regularly in the business of receiving goods on consignment for the purpose of sale. If a factor sells at an increased commission in consideration of his guaranteeing to the principal the collection of the price, he is known as a *del credere* factor. Factors have far greater implied powers to sell than ordinary agents. They may sell in their own name, and may fix the price, time of delivery and other terms; they can sell for cash and receive payment, or sell on credit and take a draft or note in payment. Moreover, they may pledge the goods to secure advances made by them to the principal, but not otherwise. Purchasers without notice take good title tho the factor sells contrary to instructions.

Under the Factors Acts enacted in England, New

York, and in many of the states, a purchaser or pledgee of such goods for values, believing the goods to be the property of the factor, is protected, so that the owner cannot reclaim the goods except on payment of the amount advanced by the third person to the factor. The act changes the law by extending to pledgees protection which was already given to innocent purchasers for value. Of course the factor is liable to his principal for any sale or pledging of the goods in violation of his instructions or authority, except that he may sell, after reasonable notice, to reimburse himself for advances made on the goods for which he has a lien, tho against the instructions of his principal.

17. *Brokers*.—Brokers differ from factors in that they have no possession of the property which they sell. They, therefore, cannot receive payment except when expressly authorized or when custom or a prior usage as between the same parties permits; furthermore they cannot sell in their own name. The special reasons, therefore, for protecting purchasers or pledgees from factors do not apply to purchasers from brokers; the general principles of agency, as heretofore discussed, apply to them.

18. *Auctioneers*.—An auctioneer is an agent of the vendor until the hammer falls. Thereafter he represents the purchaser also, at least for the purpose of making a memorandum sufficient to satisfy the Statute of Frauds. He must follow the advertised terms of sale. He may sell only for cash unless the

terms of sale provide for the granting of credit. He may receive the price or deposit in cash at the time of the sale and if it is not paid, sue for it in his own name. He has no implied authority to sell with warranty.

19. *Lawyers.*—A lawyer is his client's agent to prosecute legal actions and proceedings and perform other legal services. His implied authority in all legal actions and proceedings is very broad, including the power to determine all the usual steps in the litigation, other than a settlement or discharge of the cause of action. He must have express authority to compromise and settle a case. His client is entirely in his hands so far as the determining of all matters of procedure or of remedy is concerned, and is bound by what his lawyer does in these matters.

20. *Rights and liabilities of an undisclosed principal.*—If an agent, with actual authority to represent a principal, makes a contract with a third party in his own name but actually in behalf of his principal, a complicated situation results which has caused a great deal of controversy among lawyers. It is settled law, however, irrespective of disputes among lawyers and legal writers, that a true contract exists between the undisclosed principal and the third party, so that each may hold the other for breach of contract, the agent acting as the representative of the undisclosed principal in the making of the contract.

The third party, upon discovering who the principal is, may sue him or the agent at his election. He

may hold the agent because the agent pretended to act for himself, and is therefore estopped from denying his personal liability if the third party elects to hold him. The starting of a suit, even the recovery of a judgment and the issue of execution thereon against the agent, is not an election barring an action against the principal, if the third party does not discover the identity of the principal until later. If the principal sues the third party on the contract, the third party may set up any defense, off-set or counterclaim which he could have set up in an action brought against him by the agent. This is also the result of estoppel arising out of the false representation of the agent by which his principal is bound.

21. *Is the agent's misrepresentation legal fraud?*—Some cases hold that, if the agent affirmatively states that he is acting as principal and not as agent for his principal when he knows that the third party, for personal reasons, will not deal with his principal, the misrepresentation is fraud which gives the third party the right to rescind. It is settled, however, that he cannot rescind in the usual case where nothing is said as to the third party's objection to the principal. But the falsehood and its effects are the same in both cases.

The better and prevailing view is that the contract cannot be disaffirmed for fraud because no damage results. The third party is fully protected by his right to hold the agent, and his right to all defenses,

off-sets and counterclaims against the agent in case he is sued by the principal. At most he is injured only in that he is tricked into a legal relation with a person whom he does not like, an injury to his feelings only; therefore, there is no fraud in the legal sense.

22. *Exceptions to doctrine of undisclosed principal.*—For technical reasons it is held that the doctrine of undisclosed principal does not apply to contracts under seal or to negotiable instruments. This is another application of the old principle that these instruments are something more than evidence of the contracts; they are in a sense the contracts themselves, and therefore, no one not appearing within the limits of the instrument can be held liable on it.

In the case of negotiable instruments certainly, and no doubt also in the case of contracts under seal, where the contract has been carried out by the third person and the principal has received the benefits of his performance, the principal may be held in *assumpsit* or implied contract. Otherwise we would have the situation of a real beneficiary of a third person's performance of his contract receiving all the benefits without any liability, a result which even the technicality of ultra legal learning could hardly accept.

Another limitation upon the doctrine which is rather indefinite and obscure in its application is that the action of a third party against an undisclosed principal is subject to the state of accounts between

the principal and the agent. Some cases indicate that if the principal has paid the agent for the goods the third party must look to the agent alone. This seems to be the prevailing American doctrine, which is based on a dictum in an early English case. The later cases in England repudiate this dictum and limit the doctrine to cases where the third party has represented expressly or by his conduct that he has settled with the agent, thereby inducing the principal to pay the agent. The third party is then estopped from denying such settlement. This is sound, but the American doctrine is unintelligible.

23. *Notice to agent is notice to principal.*—Anything brought to the attention of an agent in connection with the performance of his agency which is material to the matter with which his agency is concerned is notice to the principal. The true reason for this is that the agent represents the principal for all material purposes connected with the transaction, and the principal is, therefore, bound in the same way by notice to his agent of any matter which is material to the transaction as tho he had received it in person.

In any case it is settled that notice to an agent while acting adversely to his principal, or in fraudulent collusion with a third person, does not bind the principal. The agent is not acting for the principal in such case of a wilful tort committed by the agent for his own purposes and not in performance of his agency. The principal is not liable for the tort, nor in the corresponding case is he chargeable with notice.

REVIEW

Tell when a real estate broker has earned his commission.

Explain the status of an agent who acts simultaneously for both parties.

Outline the obligations of an agent to his principal.

Give some illustrations of the type of services that an agent may delegate to another.

Discuss the rights and liabilities of an undisclosed principal.

CHAPTER XVII

PARTNERSHIP

1. *Legal nature of partnership.*—Partnership, though a common form of business organization, is legally one of considerable risk. It exposes to loss not merely a partner's investment in the business, but his entire individual resources thru the dishonesty, short-sightedness, or even misfortune of a co-partner. At law the partnership and the partners are one.

If three men form a partnership to carry on a certain business, the rights acquired and the obligations assumed in its operation are the joint rights and obligations of the three partners. It is not unusual to find that partners speak of the *firm* as something apart from themselves, as if the partnership constituted a distinct person. The law, however, does not recognize the firm as a separate legal entity, but only as the partners acting jointly.

A joint owner of land or personal property can sell or encumber his own share only, but one partner alone can transfer firm property or make a contract on behalf of the partnership, against the will of his co-partners, which will bring disaster and ruin to his associates. It is of the highest importance, therefore, for a business man either to avoid entering into the

partnership relation or else to choose his associates with the utmost wisdom.

To be safe one must avoid even the appearance of partnership, for if one holds out another as a partner or acquiesces in the other's representation that they are partners, third persons who act in reliance upon such appearance can hold them both liable as partners.

2. *Partnership and joint ownership.*—The Uniform Partnership Law as adopted in New York provides that a partnership, as between the members thereof, is (a) the association, not incorporated, of two or more persons (b) who have agreed to combine their labor, property and skill, or some of them, (c) for the purpose of engaging in any lawful trade or business, and (d) sharing the profits and losses as such between them.

Joint ownership of property which is used for profit does not necessarily make the co-owners partners. Two persons may own and operate a farm, an apartment house or a ship without becoming partners so long as the income is in substance the *return from property* rather than *profits of a business* carried on in common with a view to profits.

A playwright and a producer may unite to compose and present a play and divide the profits without becoming partners for there may be no community of interest in any property, the playwright continuing to own the play and the producer to own the scenery and costumes. But if the playwright

should *contribute* the play and the producer his money and skill to the common enterprise so that play, scenery and costumes were intended to be held as common property subject to the joint ownership and control of the two associates, and if the income were to be treated as a common fund to be divided only after expenses and losses had first been ascertained and deducted, they would become partners even tho their association might be confined to that one undertaking.

An employe or a money lender may stipulate to receive a share of the profits of a business without becoming a partner, but with a few exceptions similar to those just stated, the receipt by any person of a share of the profits of a business, *as profits*, is prima facie evidence that he is a partner in the business.

The meaning of *profits* in this connection may be illustrated by the case of a salesman who undertakes to sell the output of a factory for ten per cent of the annual net profits. If the intention of the parties manifested by their words or conduct is that the salesman is to have a proprietary interest in the profits as they accrue, i. e., to be a part owner of them, he will be deemed a partner in the business, especially if the rights of a third person are involved. But if the intention is only that the factory owners are to be indebted to the salesman for his services, the extent of the indebtedness to be an amount equal to ten per cent of the profits, no partnership exists. This may seem to be a rather fine distinction; yet the fact is

that this is often necessary since business arrangements so often resemble partnerships without there being any actual intent to create a proprietary interest in the business.

3. *Other forms of organization.*—There are other forms of organization that have some of the characteristics of a partnership, such, for instance, as joint stock companies or various clubs and societies. The joint stock company, which by the way is of little importance and gradually disappearing, takes the form of a large partnership, managed by a committee but having members equally liable for the partnership debts. A discussion of this form of organization may be found in the Modern Business Text on “Business Organization.”

In the case of clubs or societies, the members do not become individually the agents or representatives of the organization; officers are elected for that purpose. Hence no individual member is bound by the contracts of another member. A member is bound by the act of an officer but only in so far as he has expressly or impliedly authorized the officer to act in his behalf or has ratified such an act. In short, the liability of a member here is determined by the law of principal and agent.

A corporation, the predominant form of enterprise in the United States, is not a creature formed by any individuals, but created by the state or nation. It is regarded at law as a separate entity and liable, thru its officers, for its own acts; the individual stockhold-

ers in most states are not liable for its debts to a greater extent than the par value of their stock except in a few instances such as holders of national bank stock which carries double liability. The reader is again referred to the Modern Business Text on "Business Organization" for a detailed discussion of the corporation.

4. *The contract of partnership.*—Anyone competent to contract may become a partner, for partnership is a relation created by contract. The Statute of Frauds therefore applies. Under this Statute, verbal contracts which by their terms are not to be fully performed within one year from the making of the contract are void. Consequently a verbal contract to do business as partners for more than one year is ineffective; but if the parties actually begin business under such an agreement it will be treated as an agreement for a partnership terminable at the will of any partner.

Common prudence, however, requires that an agreement of such importance should be reduced to writing. Such an agreement should specify with exactness when the partnership is to begin and end, the names of the partners, the time each is to devote to the partnership, the name under which it is to be conducted, and the nature of the business to be carried on, which of course must be lawful. Moreover it should state the amount of capital each partner is to contribute, and if he is to contribute property, the value at which it is to be taken; the proportionate part

of the profits which each partner is to receive and the proportionate part of the losses which each is to bear. It is desirable, tho not necessary, that the agreement should express the understanding of the parties as to the control of the business and of the cash, bank accounts, and other property of the partnership.

The Uniform Partnership Law provides that in naming the partnership the words, "and Company," or "and Co.," must not be used unless they represent an actual partner whose name does not appear in the firm name chosen. Thus, Smith, Jones and Brown may do business as Smith, Jones & Company, but Smith and Jones may not. Nor may the name of any person not a member of the firm be used as a part of the firm name unless the partnership is the continuance of a former firm which has been engaged in interstate or foreign commerce and at least one of the partners of the old firm is a member of the new firm.

5. *Holding out as a partner.*—As has been said, a person having no intention of becoming a partner may find that the law will impose upon him the liability of a partner because of acts which it construes as amounting to a partnership or as a representation by him that a partnership exists. It is important for a man who is associated in business with others to be aware of what acts may be so interpreted. The Uniform Partnership Act provides as follows:

When a person, by words spoken or written or by conduct, represents himself, or consents to another representing him to any one, as a partner in an existing partnership

or with one or more persons not actual partners, he is liable to any such person to whom such representation has been made, who has, on the faith of such representation, given credit to the actual or apparent partnership, and if he has made such a representation or consented to its being made in a public manner, he is liable to such person, whether the representation has or has not been made or communicated to such person so giving credit by or with the knowledge of the apparent partner making the representation or consenting to its being made.

An examination of the statute shows that one will be held liable as a partner only where (a) he has either so conducted himself as to give a reasonably prudent man the impression that a partnership exists, or has consented to such conduct on the part of another person and (b) where the third party in the exercise of ordinary prudence has relied upon such misrepresentation and has been misled by it.

Knowingly permitting one's name to be used upon signs or letterheads, or permitting one's self to be referred to as a partner, or failing to give notice to persons who dealt with the firm when one is retiring from a partnership, are typical acts which the courts have treated as "holding out to the world" the existence of a partnership.

6. *Sharing in profits not always partnership.*—The Uniform Partnership Act which has been adopted in New York and several other states also provides as follows:

The receipt by a person of a share of the profits of a business is prima facie evidence that he is a partner in the

business, but no such inference shall be drawn if such profits were received in payment:

- (a) As a debt by instalments or otherwise,
- (b) As wages of an employe or rent to a landlord,
- (c) As an annuity to a widow or representative of a deceased partner,
- (d) As interest on a loan, tho the amount of payment vary with the profits of the business,
- (e) As the consideration for the sale of the good will of a business or other property by instalments or otherwise.

7. *Firm capital*.—The capital of the firm is the total sum of money and property that the partners have agreed to contribute for use in the business. Instead of contributing actual money or tangible property to the firm one of the partners may contribute the use only of property, as where a partner owning real estate contributes the use of it to the partnership, but continues to hold the title to the property as a part of his individual estate. Another partner may contribute his labor or skill. The value of such contributions may be difficult to fix, but they nevertheless constitute a part of the capital of the partnership.

8. *Partnership property*.—The property of a partnership consists not only of the capital contributed or so much of it as remains in the hands of the firm and the proceeds thereof, but also of every valuable thing which has been acquired and held by the partnership. All the property originally brought into the partnership or subsequently acquired by purchase or otherwise on account of the partnership is partnership property. Moreover, unless the contrary intention

appears, property acquired with partnership funds is partnership property regardless of whether it was acquired ostensibly as the property of the firm or of one of the individual partners in his own name. This includes the good-will as well as the tangible assets.

9. *Partnership real estate.*—The common law rule was that a partnership could not hold title to real property, because it proceeded upon the theory that title to real estate could vest only in some person and that a partnership was not a *person*, but merely a group of individuals. The consequences of this theory were avoided by the law giving effect to a deed of real property made *to a partnership under the firm name* as conveying title to the individual partners whose names happened to appear in the firm name and making them the holders of the legal title in trust for the partnership. Thus if a deed were made to “Jones & Co.,” Jones would get the title but he would hold it for the benefit of the partnership, himself and the other partners.

The Uniform Partnership Law provides that any estate in real property may be acquired and conveyed in the partnership name, so that real estate may now be held as partnership property as freely and conveniently as personal property. But unless a partnership agreement or some other writing exists which shows clearly that real estate is held as firm property, questions may arise upon the death of a partner as to whether his interest in the real estate continues as a part of the firm assets or passes to his heirs or to his

widow by way of dower. Conflicting claims may also arise between the creditors of the firm and the individual creditors of the deceased partner. The intention of the partners that the property shall be held as partnership property will ordinarily decide the question in favor of the surviving partners or partnership creditors. Thus it is clear that it is important to express such intention in a manner which will make it easy to prove, i. e., in writing. This of course applies to property which is purchased after the partnership is organized. If at the time of the organization of the partnership one of the partners contributes real estate, previously acquired by him, such real estate will remain subject to his wife's right of dower, unless by appropriate instruments she releases her dower rights.

The interest of each partner in the partnership real estate is not that of a tenant in common. Any tenant in common of real estate may bring suit at any time for a partition of the property, but a partner has no such right. Partnership real property cannot be partitioned among the partners until after the firm has been dissolved and all of the firm debts paid.

10. *Partner's interest in firm property.*—All the members of the firm are interested in the whole of the partnership property, but no partner can claim the ownership of any particular part or any particular chattel belonging to the firm. They are neither joint tenants nor tenants in common. If they were joint tenants, the share of one partner would upon his

death go to his surviving partners for their individual use, but in the case of the death of a partner his interest in the partnership property passes to his surviving partners *only for the purpose of winding up the firm*. After the firm debts are paid, the next of kin or legatees of the deceased partner become entitled to his net share of the partnership property. A partner's interest in the firm property is also unlike that of a tenant in common because a tenant in common may transfer his interest and his transferee becomes a tenant in common with the remaining co-owners, but the attempted transfer by a partner of his interest in the firm property, instead of substituting his transferee as a partner, operates merely to cause a dissolution of the firm. In fact the partners' interest in the firm property can best be stated in the words of the Uniform Partnership Law as follows:

A partner is co-owner with his partners of specific partnership property holding as a *tenant in partnership*. The incidents of this tenancy are such that:

(a) A partner, subject to the provisions of this chapter and to any agreement between the partners, has an equal right with his partners to possess specific partnership property for partnership purposes; but he has no right to possess such property for any other purpose without the consent of his partners.

(b) A partner's right in specific partnership property is not assignable except in connection with the assignment of the rights of all the partners in the same property.

(c) A partner's right in specific partnership property is not subject to attachment or execution, except on a claim

against the partnership. When partnership property is attached for a partnership debt the partners, or any of them, or the representatives of a deceased partner, cannot claim any right under the homestead or exemption laws.

(d) On the death of a partner his right in specific partnership property vests in the surviving partner or partners, except where the deceased was the last surviving partner, when his right in such property vests in his legal representative. Such surviving partner or partners, or the legal representative of the last surviving partner, has no right to possess the partnership property for any but a partnership purpose.

(e) A partner's right in specific partnership property is not subject to dower, curtesy, or allowances to widows, heirs, or next of kin.

From the above the reader will understand the nature of a single partner's title or interest in the specific assets of the partnership. Let us next consider the partner's relation to his co-partners and to the business as a whole.

REVIEW

State why there is legally considerable risk in a partnership form of enterprise.

Distinguish between a partner and a joint owner.

Explain the legal status of a club member.

Outline what constitutes "holding out" as a partner.

Describe a partner's interest in firm property.

CHAPTER XVIII

RIGHTS AND LIABILITIES OF PARTNERS

1. *Good faith.*—A partner's relations are in the main what he and his co-partners have agreed upon in the contract of partnership, but in the absence of special agreement, the law fixes their relations. No person can become a member of a partnership in any manner without the consent of all the partners.

The first duty of a partner is to act in the highest good faith toward his co-partners and toward the legal representatives of any deceased partner, to give them on demand true and full information of all things affecting the partnership, and to devote his time and attention to the partnership affairs unless he is relieved from so doing by agreement with his co-partners. He is under a like obligation to account to the partnership for any benefit and hold for it as trustee any profits derived by him without the consent of the other partners from any transaction connected with the formation, conduct, or liquidation of the partnership or from any use by him of its property. The partnership books should be kept at the principal place of business of the partnership and every partner is entitled to inspect and copy any of them at any reasonable time. It is the corresponding

duty of each partner to keep an honest and full account of all his transactions connected with the business of the firm. In the absence of an agreement a partner has no right to give his time, skill or efforts to any other business to the prejudice of the partnership affairs nor to carry on any business in competition with the firm.

2. *Management of the partnership.*—All partners have equal rights in the management and conduct of the partnership business and no partner is entitled to extra remuneration for acting in the partnership business except that a surviving partner is entitled to reasonable compensation for his services in winding up the partnership affairs. Any difference of opinion arising about ordinary matters connected with the partnership business may be decided by a majority of the partners, but no act which is in violation of any agreement between the partners may be done rightfully without the consent of all the partners. Before acting in any important matter a partner should consult with his co-partners unless such consultation has been dispensed with by agreement or unless the circumstances are such as to give no opportunity for a consultation.

3. *Application of firm assets.*—Each partner has the right to have the partnership property first applied to the payment of firm debts and liabilities. No partner without the consent of his co-partners can use partnership property in payment of his own debts or for his own purposes. If one of the partners, in

aid of the partnership, has made any payment or advance beyond the amount of capital which he agreed to contribute, he is entitled to interest from the date of the payment or advance and to have the sum so advanced returned to him before any distribution of profits takes place. He is, of course, entitled to be reimbursed for proper payments made by him on account of the firm if they were not made necessary by his own misconduct. After these advances are met and the firm debts are paid, each partner, in the absence of special agreement, shares equally in the proceeds of the firm and must contribute equally to the losses sustained by the partnership.

Just as a partner has a right to be indemnified for money which he has been compelled to pay out in connection with the firm business, so he or the partnership must, if necessary, contribute to an individual loss sustained by any partner thru a wrongful act committed by the partnership or its agents. The ordinary rule is that where several persons jointly engage in an illegal act resulting in a loss which falls upon one of the wrongdoers alone, the law will not compel his associates to contribute their proportionate share of the loss. The reason is that the law will not interfere to adjust the rights of wrongdoers among themselves. However, this is not applied strictly to a partnership. If a partner sustains an individual loss because of an illegal act of the partnership which was not brought about by the fault or wrongdoing of the losing partner, the illegality will

not defeat his claim for contribution from his co-partners.

4. *Enforcement of obligations among partners.*—

A peculiarity of the legal relations existing among partners is found in the fact that if a partner violates his obligation to his associates, this does not give them a right to sue him. It may entitle them to damages or to an accounting, but the enforcement of their rights is in general postponed until the dissolution of the partnership and the winding up of its affairs, at which time all claims and controversies among the partners connected with the firm are taken into account.

5. *Power of partner to bind firm by contract.*—

Every partner is a general agent of the firm for the purpose of its business. As long as the partner is apparently carrying on firm business in the usual way the person dealing with him has the right to assume that the partner has authority to act for the partnership in the matter in hand. The partnership is bound by such an act unless the partner actually had no authority to act for the partnership as he did in the particular matter *and the person dealing with him knew it*. An act of a partner which is not apparently for the carrying on of the firm business in the usual way does not bind the firm unless it was authorized by the other partners. Hence it becomes important for us to consider what sort of acts are or are not apparently for carrying on the firm business in the usual way.

6. *The scope of the business.*—To answer this question we must first inquire whether we are dealing with a partnership engaged in trade, in manufacture, in farming or in practicing law or medicine. Obviously, the business carried on by these different firms varies greatly and the powers of a partner vary accordingly, for he has no power to bind the firm to third persons in any matter outside the scope of the business ostensibly carried on by the partnership. By “scope of the business” is meant the limits of that kind of business fixed by the usual custom of the place and trade. To put it another way, a partner can bind his firm to third persons by such acts as are reasonably adapted to carrying on the apparent business of the partnership and do not go beyond the general usages or customs of other firms engaged in the same or a similar business.

Bearing in mind that the partner is an agent and the partnership a principal, that which has been said under the heading of principal and agent is applicable to the powers of a partner, especially as to the apparent scope of the employment, secret limitations upon the agent’s authority, and the ratification of unauthorized acts, either by express words, by acquiescence or by having adopted or ratified previous acts of a similar nature.

Each partner has power to employ agents and servants for the firm, to employ an attorney, to execute or indorse negotiable paper for partnership purposes but, subject in each case to the tests given

above. For example, a partner in a trading partnership could bind his firm by a promissory note or trade acceptance given for the purchase price of a large consignment of goods apparently adapted to use by the firm, but a firm of doctors or lawyers would not be bound by a firm promissory note so given unless it was authorized or ratified by the other partners. It is not the ordinary practice of such firms to use the firm credit in that manner. A partner may borrow money for the firm and bind the firm for its repayment even by giving a chattel mortgage on the firm property. This is true, even tho he misappropriates the money, provided that the borrowing was apparently a reasonable and ordinary incident in carrying on the firm business and the lender believed it to be a partnership act.

Hence a third party may safely pay to any partner money due the firm or give a note or settle an account with him, or even compromise a dispute with him if it arises out of the usual course of the partnership. But if it is an *unusual* controversy, such as a damage suit for negligence or the settlement of litigation actually pending, the co-partners would be bound by such a settlement only if they had expressly authorized it. Nor can one partner bind his co-partners by consenting to arbitrate a claim made by or against the firm.

7. *Instruments under seal*.—It is also the general rule that one partner cannot without express authorization bind his co-partners by an *instrument under*

seal. In general, therefore, a deed, lease or mortgage of real estate made by a firm should be signed by all the partners as joint parties. One partner cannot bind the others thereby unless he has been so authorized *in writing and under seal*.

There are exceptions to the rule. One partner may bind his firm by a *general release*, i. e., an instrument bearing a seal which formally releases and discharges all claims of the firm against the person to whom it is given. An instrument under seal signed by a partner without authority may be ratified by the co-partners and thus become binding on them, as where the firm occupies property under a lease taken without authority by one of the partners. In most cases where a seal, tho unnecessary to the validity of the instrument, nevertheless is used, the courts will disregard the seal as being surplusage and give effect to the instrument as a simple contract. For example, the addition of a seal to a promissory note or to an ordinary business contract, either of which is legally valid without a seal, would not affect the validity of the instrument as binding on the other partners.

8. *Fixed property*.—In selling property of the partnership, while each partner has implied power to sell firm property when that is the customary way to carry on the firm business, no partner has implied power to sell *all* the property of the firm or to do any other act which would make it impossible to carry on the ordinary business of the partnership. A partner in a mercantile house might sell the entire

stock of goods, for it is the firm's business to buy and sell goods. But he could not sell the store fixtures or the truck used for deliveries for it is not the firm's business to buy and sell store fixtures or trucks. Their sale might prevent the firm from carrying on its business.

Again, one partner alone cannot sell or convey real estate held as partnership property for two reasons. In the first place, real estate can only be sold by a deed which must be under seal. In the second place, it is not the ordinary business of any but real estate dealers to sell real estate. Even in the case of a partnership dealing in real estate the technical nature of a transfer of real estate ordinarily makes it desirable, at least, that a deed should be signed by all the partners.

9. *Individual debts.*—It is of course outside the apparent scope of a partner's authority to use firm money or a firm check for the payment of his individual debts or to pay such debts by the sale of firm property. Hence a third person will get no title as against the firm to money or property so transferred. But if a partner should draw a firm check to himself and then indorse and deliver it to a third person in payment of an individual indebtedness, unless the latter had reason to suspect the partner of misappropriating firm money, he would have the right to assume that the partner was authorized to withdraw the money from the firm and such payment would bind the firm even tho it was in fact a misappropriation of

firm money. The reasoning is that the partner has *apparent control* of the partnership funds, and the third party is a *bona fide holder* of the money.

A partner has no apparent authority to use the firm name as a surety, to indorse commercial paper or to pledge the firm credit *for the accommodation* of another person, even tho a customer of the firm. Here again, however, the partnership purposes must be considered; such a contract might be a legitimate incident to a particular firm's operation. In that case it would be valid.

10. *How a partner's authority is shown.*—It must not be forgotten that the third party cannot safely rely upon the representations made by a partner as to the extent of his authority. Should it become necessary to prove that a partner was authorized to do a specified act his representations that he had such authority would not be admissible evidence. For instance, if Smith asserts that he has certain authority to represent Jones, Smith's assertions are not binding upon Jones. The best evidence in such case is a statement or admission by Jones. Consequently, whenever there is the slightest doubt as to a partner's authority to bind his co-partners by a particular act or contract, confirmation of his authority should be obtained from the co-partner upon whose financial responsibility reliance is to be placed.

Representations or declarations by a partner as to his authority must not be confused with statements or admissions made by him concerning firm business

when he is actually acting within the apparent scope of the partnership business. Such admissions or declarations are binding upon the firm, and it will not be permitted to contradict them later to the disadvantage of a third person who has believed them and acted upon them. Thus a statement by a partner of a firm of stock brokers to the effect that he was authorized by his co-partners to accept money for investment in mortgages upon real estate would *not* be binding upon his co-partners. But if the partners were actually engaged in that business and one of them represented to a third person that money given him to invest in a particular mortgage had actually been so invested, such representation would be evidence against his co-partners for it would be incidental to the ordinary course of business of the firm.

11. *Firm bound by wrongful act of partner.*—We have been considering those acts of a partner which may give third persons contract rights against the firm. But a partner, by wrongful acts, may give third persons claims for damages against the firm. A partner's wrongful act or wrongful omission to act in the ordinary course of business of the partnership, causing loss or injury to third person, gives him a right of action, not only against the wrongdoer but also, and to the same extent, against his partners.

In New York and some other states this rule of law extends even to the right to arrest and imprison the innocent partner when the law gives the right of arrest against the wrongdoer in a civil action for per-

sonal injury or injury to property. His personal innocence is no defense. This rule rests upon the theory that the contract of partnership constitutes all its members agents for one another, and that when a loss must fall upon one of two innocent persons, he must bear it who has been the occasion of the loss or has enabled another to cause it. The wrongful act of the agent is the act of his principals, if done in the course of his agency, tho not directly authorized by them. This rule extends to liability for fraud, for slander and for misappropriation of funds, but does not impose criminal liability upon the innocent partner. For example, if one partner publishes a criminal libel upon a customer, the customer could bring suit against both partners or against the innocent partner alone; he could, in New York at least, have the innocent partner arrested and held to bail in the civil action but criminal proceedings would lie only against the guilty partner.

12. *Extent of partner's liability.*—Each partner is personally liable for the entire amount of a firm obligation, regardless of his proportionate interest in the firm. His individual property may be levied upon to pay a judgment obtained against the partners. The creditor may, at his option, collect the entire amount from one partner alone. In that case the partner's only relief is to compel his co-partners to contribute their share as fixed by the partnership agreement. This can be done only upon the dissolution of the firm and final accounting.

13. *Rights of firm creditors.*—In almost every case of partnership insolvency two sets of creditors appear, the firm creditors and the creditors of the individual partners. Their interests may conflict because, as we have seen, the firm creditors have the right to effect the seizure, not only of the firm property, but also the individual property of any or all of the partners. They may even proceed first against the individual property of a partner without attempting to satisfy their claims out of the partnership assets. On the other hand a creditor of an individual partner can seize or levy upon firm property only in subordination to the rights of firm creditors. In most states he can levy upon the partner's interest in the firm, but all he is entitled to is the share of the debtor partner in the net proceeds of the partnership after the partnership affairs are wound up and all the partnership debts paid. The firm creditors thus have a decided advantage over the creditors of the individual partners in any case where resort to the firm assets is necessary to satisfy the claim of the individual creditors.

The common law places a premium upon diligence. The first creditor to effect a seizure of his debtor's property acquires a prior lien upon it which entitles him to apply it to the satisfaction of his claim, regardless of whether his claim arose before or after other claims and regardless of whether or not anything is left for the other creditors. It is the doctrine of first come, first served.

Relief from the hardships of this rule is found in two

directions. The National Bankruptcy Act proceeds upon the theory that equality is equity. It restrains the too eager creditor and provides for the orderly liquidation of the assets of the bankrupt and the payment of the creditors pro rata. The rights of creditors to have their debtor declared a bankrupt should be thoroly understood by all concerned and a study of the National Bankruptcy Act is advised. In most states the failing debtor may make a voluntary assignment for the benefit of creditors. It then becomes the duty of the assignee to liquidate the property and distribute the proceeds pro rata. In such cases the conflicting rights of firm creditors and individual creditors have given rise to many rules which cannot be profitably considered here and require in each case the advice of counsel for their application.

14. *Individual creditors.*—The creditor of an individual may proceed against the individual property of his debtor by attachment or execution, regardless of the existence of the firm. It was formerly the rule that a sheriff under such process could seize the firm chattels but the purchaser at the sheriff's sale would not get title to the chattels as is ordinarily the case; he acquired only a right to hold possession of the chattels until the debtor's partners should account for and pay over to the purchaser the debtor partner's net share in the partnership.

Under the Uniform Partnership Act the inconvenience of this procedure is done away with in the

states where the act has been adopted. The creditor, under it, may procure from the court a "charging order" which, without interference with the property of the firm, charges the share of the debtor partner with payment of the debt. If necessary, the court will appoint a receiver of the debtor partner's share for the purpose of collecting it and satisfying the judgment.

15. *Dissolution*.—The dissolution of a partnership is the change in the relation of the partners caused by any one of them ceasing to be associated in the operation of a business. This must be distinguished from the winding up of a business, in which event the partnership continues until the winding up of the partnership affairs is completed. Dissolution is caused automatically by the death or bankruptcy of any partner, by termination of the period or undertaking specified in the partnership agreement, or by the withdrawal of any partner, even in violation of the partnership agreement. But a court may decree a dissolution whenever a partner becomes incapable of performing the partnership agreement or is guilty of misconduct which affects prejudicially the carrying on of the business, when he persistently violates the agreement, or when other circumstances require it. Except so far as may be necessary to wind up firm affairs or to complete transactions begun but not finished, dissolution terminates all authority of any partner to act for the partnership.

However, if a partner exceeds his authority his

former co-partners may still be liable to any one who has formerly dealt with the partnership and who deals with the partner without notice of the dissolution. To avoid this contingency the fact of dissolution must be advertised in a newspaper of general circulation in each place in which the partnership business was regularly carried on and actual notice of it given to all persons who have extended credit to the partnership. Whenever a partner retires from a firm the only way he can protect himself from liability for the subsequent acts of his former partners is by giving notice as indicated above. The importance of doing so is obvious to every business man.

16. *Final accounting.*—The right of each partner to full information and to a complete accounting from his co-partners of all matters affecting the firm business has been emphasized. This may be compelled by suit during the continuance of the firm, but ordinarily, when matters have reached the point where litigation starts between the partners, a dissolution follows to which the accounting is a necessary incident. The penalty for failing to keep full and accurate accounts is that every uncertainty caused by it will be resolved against the accounting partner.

The first step in a final accounting is to collect the debts due the firm and liquidate its assets. The second step is to ascertain the debts of the firm to outsiders; these must be paid first. Next the partners should be paid, with interest, money advanced to the firm aside from contributions to the firm capital, fol-

lowed by the distribution of capital contributed without interest or so much as is ratably due him on that account.

If there is still a residue it will be distributed to the partners as profits in accordance with the partnership agreement. If, on the other hand, the assets are insufficient to pay the firm debts, the partners must contribute to the deficiency according to the profit and loss sharing ratio. The details of this procedure are of interest from the accounting angle mainly and will not be discussed here.

If one partner is insolvent, the solvent partners must make up his share in the same proportion. Of course, if the partners have agreed to a different way of distribution their intentions will govern the final accounting unless the result would be prejudicial to the creditors.

In connection with the final accounting it is essential for the partner charged with the winding up to consider whether the good-will of the business may not be a valuable asset. If it is, he must, as in the case of any other valuable asset, be diligent to cause its sale for the best price obtainable. Failing in this duty he may be charged with its value. When one partner has died or withdrawn, the surviving partner or partners may desire to continue the firm business. If they have not provided in the partnership agreement for the use of the firm name by the surviving partners, the firm name is regarded as a part of the good-will of the business and the purchaser of the

good-will obtains the sole right to do business as the successor of the firm. The winding up is simplified if the partners have agreed that not only the firm name but the good-will also shall vest in the surviving partner or partners.

17. *Limited partnerships*.—Something should be said of certain special arrangements which give rise to different classes of partners and partnerships. We have considered hitherto general partners or those who were expected to take a full share in the business. A partner who contributes capital, but takes no part in the business and whose relationship to the business is concealed, is called a *silent* or *dormant* partner. He is liable to the same extent as an ostensible partner. If he takes an active, tho concealed part, in the business he is called a *secret* partner. His liability in either of these cases is that of a general partner.

By statute in New York and some other states, provision is made whereby one may become a *special* partner with liability limited as in a corporation to the loss of the capital contributed by him. A partnership having such a member is known as a *limited* partnership. Such a firm must have at least one general partner with unlimited liability. The limited partner loses his protection and becomes liable as a general partner if he takes any part in the control of the business.

Limited partnerships can be formed only by filing a certificate as provided by the statute. Since the

principal purpose of such partnerships is to limit the liability of one or more partners and to preserve their rights to deal with the co-partners as an outsider could, it is now about as easy and more effective to form a corporation. In this way the liability of all the members is limited in most states to the amount subscribed. Moreover, the right of each to participate in the management while still being free to deal with the corporation and even to bring suit against it with the same facility as a non-member is preserved. Probably the ease with which corporations may now be created is the reason that very few limited partnerships are organized. One advantage, over the corporation, that the partnership still enjoys is freedom from the necessity of complying with certain legal formalities and of making frequent reports to the state or federal government.

REVIEW

Discuss the requirement of good faith in partnership relations.

Explain the power of a partner to bind the firm to third persons by contract.

Describe the extent of a partner's liability.

Distinguish between rights of firm creditors and individual creditors in case of the insolvency of a firm.

Differentiate between "dissolution" and "winding up" of a partnership.

State what a retiring partner should do to protect himself from liability for subsequent acts of the firm.

CHAPTER XIX

SURETYSHIP AND GUARANTY

1. *What constitutes suretyship and guaranty.*—A contract to pay the debt of another is a contract of suretyship. The surety may undertake to pay the debt absolutely, or he may make his promise depend on any condition he pleases, limiting his liability as in other contracts of all kinds. He usually promises to pay the debt if the debtor does not do so, and default on the part of the debtor is a condition precedent to his liability as surety.

Upon default by the debtor the surety at once becomes liable. No notice need be given him of the debtor's default in the usual case. He and the debtor may both be sued at once. Sometimes the contract provides or is construed as meaning that the creditor must attempt to collect in the usual way by action, judgment and execution before the surety becomes liable; if so, such condition must be complied with like any other condition precedent, and the creditor can sue the surety after he has exhausted the usual remedies against the debtor. This is the so-called guaranty of collection.

The term "guaranty" is very generally applied to these cases, and quite generally to the other class of

cases where default of the debtor is a condition precedent to the surety's promise. But a guaranty is merely a contract of suretyship, the term being used interchangeably with suretyship in these limited cases to which the term is applied.

2. *Contract between creditor and surety.*—A valid contract must exist between creditor¹ and surety. There must, of course, be mutual agreement and consideration. The peculiarity of the contract is that it relates to the debt or obligation of a third party, and generally, to performance by the latter. The consideration for the surety's promise is usually the giving of credit or the extension of credit by the creditor to the debtor. If such credit already has been given, then a new consideration must be paid, as where a premium is paid a surety company for its bond. The general rules of contract involving mutual assent and consideration apply to this as to other contracts; these require no elaboration at this point since they have been fully explained in the chapters on contracts.

3. *How defenses of the principal debtor affect the surety's contract.*—If the surety's promise is to pay all debts which the debtor owes, any valid defense to the principal debtor's obligation is a defense to the surety. But if the surety undertakes to pay a stated sum or perform a specified act, such defenses as infancy, insanity, ultra vires, and defective execution of a contract apparently valid, will generally not be good in favor of the surety, tho it must be stated that the cases on these questions are by no means in ac-

cord. Since the surety's promise is not expressly conditioned upon freedom from such defenses, his promise to pay, if the debtor does not, should be enforced against him, even tho the debtor can set up infancy or any other of these defenses.

Illegality of the debtor's contract, or fraud or duress rendering such contract void when made, or void because disaffirmed by the debtor, are valid defenses to the surety. In the first class of cases, the surety is liable because he is of age, of sound mind, and thus should carry out his promise, even tho the debtor be relieved. In the second class of cases, the surety cannot be held because to hold him would result indirectly in enforcing the fraudulent or otherwise wrongful transaction against the debtor who could be held by the surety on his implied promise to indemnify the surety.

4. *Discharge of surety by payment or release of principal debt.*—If the debt is paid, the surety is necessarily discharged. The creditor is not entitled to payment twice. In similar manner where the creditor releases the debtor from liability, by way of accord and satisfaction, compromise or settlement of any kind, the surety is discharged. A release of only a part of the debt, however, discharges the surety only to a corresponding extent. If the right to hold the surety is expressly reserved, the courts will construe the release or other discharge as a covenant not to sue the debtor so that the debt may continue and the surety be held liable. In that case the surety, on

paying the debt, may at once sue the debtor for indemnity, making the settlement with the creditor of little practical value to the debtor.

5. *Extension of time by creditor discharges surety.*

A binding extension of time to a debtor by a creditor discharges the surety. Such an extension of time is a material modification of the original indebtedness for which the surety is obligated, and, therefore, the surety's promise no longer applies. He contracted to be surety for the payment of the debt payable at the original date; not for the debt payable at a later date. The risk he runs may be increased, and therefore he is discharged.

It should be noted that the extension of time must be by valid contract supported by a good consideration. A mere gratuitous promise to give more time, followed by refraining from suit during that time does not release the surety, as it amounts merely to a delay in enforcing the claim; a delay does not result in changing the surety's obligation in any way. Consent by the surety to the extension in advance, or a promise to continue as surety after the extension, prevents the surety's discharge in these cases.

In several states it is held, or stated by the courts, that an extension of time for an indefinite period does not discharge the surety. But, if the extension may be interpreted as meaning a reasonable time, an enforceable extension by contract exists, and the surety, under the general rule, would be discharged. It has been so held in a few cases. If the extension

contract may be voided for fraud or other valid defense, or is void because of illegality of consideration, the surety is not discharged. The payment of usurious interest, however, does not, according to the prevailing law, invalidate the extension and the surety is therefore discharged.

6. *Reservation of right to hold surety prevents his discharge.*—The reservation of right to hold a surety prevents his discharge in cases of extensions of time as of releases. The surety's rights against the debtor are not affected, as the surety may be held or may pay the debt at the original date of maturity, and then sue the principal debtor for indemnity.

It may fairly be said that all of the well-settled law, to the effect that a surety is discharged by an extension of time, is based on an exceedingly technical foundation. Actually, the original indebtedness continues. The change in date of maturity ordinarily will benefit rather than hurt the surety, and if he were approached in advance, he would probably welcome the extension. A rule permitting him to set off any actual damage sustained by him as a result of the extension would be more in accord with justice and common sense.

7. *Surrender of collateral security discharges surety pro tanto.*—The rule that the surrender of collateral security discharges the surety to the extent of its value arises out of the surety's equitable right of subrogation. The doctrine of subrogation, or substitution, applies where a man pays a debt not his own

and yet is not a mere volunteer or intermeddler. He assumes, in this instance, the position of the creditor to whom the money is paid and is given the creditor's rights to any security held against the debtor. A surety comes squarely within this rule. He, therefore, gets the benefit of any security on the debtor's property, real or personal, which the creditor may have, such as a mortgage on the debtor's real or personal property, or collateral security in the form of stocks or bonds held by the creditor.

The loss or surrender of such security by the wilful act or negligence of the creditor is regarded as a wrongful interference with this equity, and the surety will be discharged to the extent of the value of the security surrendered. On the other hand negligent failure to act, as failure to enforce a lien or mortgage on the debtor's property, failure to insure, failure to prove the claim against the estate of a deceased creditor, will *not* discharge the surety. His negligence or wilful wrong must be of an affirmative nature and not simply an omission.

The cases holding that surety is not discharged *pro tanto* in these situations have little to recommend them. Tho the surety can protect himself in these cases by paying the debt and enforcing the creditor's rights against the debtor, it would seem natural that he should leave this to the creditor who has the primary right, and in many cases failure to act has been held to be negligence which will discharge the surety to the extent of the resulting loss. Failure to record

a mortgage resulting in the loss of it by the surety, failure to give notice of dishonor of negotiable paper so that the indorser cannot be held where the paper is held as collateral, discharges the surety *pro tanto*.

8. *Variation or alteration of principal debtor's contract*.—If a change of the principal debtor's contract modifies the surety's contract in any substantial respect, the surety is discharged; otherwise, a new contract would be forced on him without his consent. He cannot be held according to the terms of his original contract since it is discharged by the change in the principal debtor's contract, the new contract taking the place of the old. Of course, the change must be material, and it must be a change in the obligation of the debtor which the surety guarantees. Thus a guarantor of a tenant, guaranteeing that he will pay his rent, will not be discharged by changes in the lease which do not affect the amount or time of payment of the rent.

The fact that the change may benefit the surety rather than increase his risk will be immaterial and he will be discharged if there is any possibility that his risk may be increased by the change. But discharging the debtor in part, by reducing the amount of the debt, or reducing the price he is to pay, can certainly do the surety no harm, and he is not discharged in such cases.

Changes contemplated and provided for by the original contract do not discharge the surety. Illustrations of this rule are found in the changes in plans

and specifications of a building contract permitted by the contract on stated terms, or again, the subleasing of leasehold premises by a tenant with the landlord's consent, expressly provided for in the original contract or lease.

Performance of the contract by the principal in a different way from that provided by the contract discharges the surety if it causes or may cause loss to him. Payment to a contractor before the money is due, therefore, discharges the surety. It may well result in failure of the contractor to perform his contract, to the surety's loss. But where the departure from strict performance is immaterial, doing no harm, the surety remains liable. For example, where an architect's certificate is required under a contract, but payment is made without its production, and it appears that the contractor's work had been fully performed, the departure is held to be immaterial and the surety is liable.

9. *Tender of payment and rejection by creditor.*—Tender of the debt and rejection thereof by the creditor discharges the surety. This act is equivalent to performance so far as the surety is concerned, and the creditor cannot reject performance by the debtor and still retain the security of the surety's promise. Much the same principle is involved in case of tender by a mortgagor of the mortgage debt discharging the mortgage, and tender of a debt secured by pledge discharging the pledge so that the pledgor may recover his property from the pledgee.

10. *Failure of the creditor to sue debtor.*—When the creditor fails to sue the debtor, it has no effect ordinarily, as no binding extension of time is given. But, if after the debt is due the surety demands that the creditor sue the debtor, and the creditor fails to do so for an unreasonable time, the surety is discharged in New York and several other states, provided it appears that the claim has been lost in whole or in part in consequence of the delay. In several other states the same law has been provided by statute. Elsewhere the doctrine has been rejected by the courts.

11. *Notice to surety of debtor's default.*—Notice to surety of debtor's default is not generally necessary unless expressly made a condition precedent to the surety's liability. In cases of guaranty of acts which are indefinite as to time of performance it is established by weight of authority that notice must be given the surety, if performance is of such a character that the creditor would have knowledge of it and the surety would not. Many cases, however, hold to the contrary. Failure to give notice, which, when required must be given in a reasonable time, must be set up and proved as a defense by the surety.

12. *Fraud or duress by debtor or creditor to surety.* If the creditor is not a party to the fraud or duress, knowing nothing of it, his right to hold the surety on his contract cannot be affected by the wrongful acts of the principal debtor.

But the creditor's fraud, or his silence as to facts

so material to the risk that withholding them by the creditor amounts to affirmative fraud to the surety, good faith and fair dealing demanding their disclosure, gives the surety the right to avoid the contract on the grounds of fraud. Thus when an employer fails to disclose former acts of dishonesty on the part of an employe whose honest performance of his work is being insured under a fidelity bond, the bonding company cannot be held by the employer in case of a subsequent act of dishonesty by the employe.

The same principle applies when the bond has been made before knowledge of a subsequent act of dishonesty is obtained by the employer. The concealing of such an act, and permitting the employe to continue in his work is a fraud that will discharge the surety from liability should he avail himself of the defense. Ignorance due to negligence is not enough. There must be actual fraud, and therefore the employer must have knowledge of the act of dishonesty.

13. *Termination of the contract.*—A contract of suretyship, like any other, ends when it is performed or discharged thru any one of the ways by which contracts in general are terminated. It cannot be revoked by the surety nor will it terminate at his death when it is to continue for a definite period, or for a period capable of being reduced to a definite period, provided the consideration for the contract was given to cover future transactions to be performed during the life of the contract. Thus a contract by a father to guaranty performance by his son as underwriter

in consideration of his being admitted to Lloyd's was held to bind the father's estate many years after his death.

Again the promise of the surety may be to guarantee the future sales or credits, the consideration for each being the sale or credit in each case. Such a promise is really a series of offers accepted in each case when the sale is made or the credit given. Such offers like all others may be revoked at any time and the death of the surety will of course revoke all that have not been accepted. No contract in fact exists except as to the transactions which have been executed. But where a consideration is given in advance, or the contract is under seal, the surety may nevertheless revoke if his obligation is not fixed in duration or cannot be made definite by the happening of some future event. It is a contract at will, and may be ended at any time on notice.

There is no doubt that a fidelity bond may be revoked when an act of dishonesty has been committed by the employe. If not expressed it is a clearly implied term of the contract.

14. *Rights of the surety—reimbursement.*—A surety has an action against the principal debtor for any amount that he is compelled to pay as surety in behalf of the debtor. This action is on an implied promise to indemnify the surety.

15. *Surety's right of contribution.*—When there are two or more sureties, and any one of them pays more than his share of the debt, he has a right of con-

tribution against the others, so that the burden may fall equally on all. This is based on the obvious justice of making all who are equally liable on the same obligation share the burden equally. It originated as a remedy in equity, but it was adopted also at law, so that the action may be brought either in equity or at law. It is immaterial whether the co-sureties were obligated as such in the same or different instruments, or whether they knew that there were other sureties or not. The doctrine is based on principles of justice and does not turn on any supposed implied promise.

The fact that one surety is no longer liable when payment is made by another does not relieve him from liability to contribution, as where the claim against him is barred by the Statute of Limitations. His liability to contribution arose when he became co-surety. The surety enforcing contribution need not have paid the entire debt. On paying more than his share of the total debt, his right at once arises.

16. *Contribution between sureties for different sums.*—Where the sureties contracted to become liable as sureties for stated maximum sums of money, contribution between them will be in proportion to these amounts. If one is surety to the extent of \$1000, the other to the extent of \$2000 they must contribute to any loss in the proportion of 2 to 1.

17. *The Statute of Frauds.*—The Statute of Frauds provides in this connection that no action shall be brought to charge the defendant upon any special

promise to answer for the debt, default or miscarriage of another person, unless the agreement or some note or memorandum thereof shall be in writing and signed by the party to be charged, or by some duly authorized agent. All contracts of suretyship are promises to answer for the debt or default of another, and therefore, must be in written form to comply with the Statute of Frauds. This provision has been included in corresponding statutes enacted in the different states of the United States.

REVIEW

Define suretyship and guaranty.

State why a binding extension of time will discharge a surety, and distinguish between it and a so-called delay.

In the case of surrender of collateral security by a creditor, explain the status of the surety.

Outline the ways in which a surety may be discharged.

Discuss the obligation of contribution among joint sureties.

CHAPTER XX

REAL PROPERTY—DEEDS AND MORTGAGES

1. *Real estate and personal property.*—Business or commercial transactions are usually concerned with personal property, and only incidentally has it been necessary in the preceding discussion to refer to land and contracts connected with it. Deeds, mortgages and leases are, however, of familiar occurrence in business operations, and it will be necessary to consider so much of the law of real estate as may be needed for an understanding of these contracts. No attempt will be made to consider at length the law of real property which represents one of the most technical branches of law. While the layman should understand the general rules governing the more frequent transactions in real estate he could not properly be advised to undertake contracts of any considerable magnitude without the advice of counsel. Not only the importance of the transactions but their relative infrequency in the usual course of business operations suggests that they should be entered upon with a more than usual degree of caution.

Real property, the subject matter of deeds, mortgages and leases, consists of land and anything affixed to it in such a way that it becomes legally a part of it.

All other property is personal property. Growing crops, trees, grass and other natural growths are physically and legally part of the land on which they grow. However, annual crops, the result of annual planting and cultivation, are by special exceptions treated as personal property for the purpose of sale. Unless specially reserved they pass with the land, when the land is conveyed. Trees and bushes and their products do not come under this exception, tho it has been held otherwise in a few cases as regards crops of fruit requiring annual care.

The significance of these distinctions lies in part in the application of the Statute of Frauds. If the thing sold is land or real property, it comes under the rules of the Statute requiring written contracts. Contracts for the sale of growing trees or perennial crops must, therefore, be in writing, tho contracts to sell cordwood or logs to be cut and delivered by the vendor from specified growing trees are good by parol. If on the other hand the things sold are personal property they are subject to the rules previously discussed.

2. *Fixtures*.—The most important subject in the law involving the distinction between personal and real property is the law of fixtures, and an understanding of this law is often required in business transactions of various kinds. A fixture in the typical case is a chattel annexed to land in a permanent way with the intent of making it part of the land. Household fixtures, including plumbing fixtures, furnaces, radiators, etc., and fixtures used in trade or

manufacture, including permanently placed or annexed machinery of all kinds, built-in show cases, shelving, etc., are typical cases of fixtures which become part of the land or building for all purposes, and therefore realty, when annexed by the owner of the premises. They pass with the land when it is conveyed or mortgaged, or when it passes by will or inheritance.

Yet all of these articles are considered as personal property belonging to the tenant when they are annexed by a tenant for years. The fact of the tenancy changes the situation. It is clear that the average tenant would not intend to annex them permanently for the landlord's benefit and the intent of the annexor, as an average man, is the test of whether or not fixtures are annexed permanently. Therefore, a tenant may sell such fixtures as personal property under the Statute; and use and dispose of them during the term in any way he likes. But if he quits the premises and leaves them on the premises at the end of the term, he cannot later come back and remove them. This is a survival of the old doctrine that anything attached becomes part of the land; this has given way generally to the modern test of intent to annex permanently. Because, too, of this doctrine of the old law, a trespasser who annexes a fixture loses all right to it, and it becomes part of the land at once.

Tenants were said at first to have a special privilege of removal which trespassers and others did not

have, but it had to be exercised before leaving the premises at the end of the term; hence, if a tenant failed to remove the fixture on moving away, he would lose it. The modern law, however, recognizes clearly enough that the tenant may take the fixture because it is his personal property. He loses it in case of quitting the premises without removing it, because coming back to remove it would involve a plain case of trespass. Mere chattels of the tenant are not affected by this rule, and the tenant may return and demand them because they have never been attached.

If the tenant takes a new lease for a further term he loses his fixtures unless he removes them beforehand, or unless he reserves them in the new lease. Some states hold to the contrary, and the development of the law is strongly in that direction. The prevailing rule is illogical and technical and will probably give way in the interest of justice and reason.

3. *Land ownership.*—The ownership of real property may be absolute or limited. The first is known in law as an estate in fee simple. On the other hand a limited ownership exists in the case of a life estate which ceases with the life of the owner or other person, or in a tenancy for years which of course terminates with the expiration of the term for which it is created. On the expiration of a limited estate for life or for years the land passes to the man who is owner of the balance of the fee as absolute owner, called a remainderman or reversioner.

The more frequent business transactions in real estate are the sale and conveyance of the property by deed, the pledging of the property as security for debt by mortgage which takes the form of a conditional sale, and finally the leasing of property to others. What is involved in these transactions may now be considered.

4. *Deeds and conveyances.*—The first and most important step from the business and legal standpoint in buying and selling real property is the contract of sale. This contract must be in writing under the Statute of Frauds. No seal is required and an agent may sign for his principal without written authority.

The contract is important because its terms fix absolutely what the deed must provide. For instance, if a warranty deed, explained below, is wanted by the purchaser he must have a provision requiring it in the contract, or he may be compelled to accept a quit-claim deed. It is important, therefore, that a layman should have competent legal aid in the preparation and execution of the contract, and that he should not regard the contract as a mere preliminary to the deed. It determines absolutely his rights when the closing of title takes place and the deed conveying the land is delivered.

Deeds must be under seal except where seals are dispensed with by statute. They must always be in writing. The form of deed generally used to-day in conveying land is the short-form deed of grant, the form being provided for by statute in most states.

If it contains the usual covenants of title it is called a warranty deed; if those covenants are omitted, it is in legal effect a quitclaim deed whether or not the word "quitclaim" appears in the words of conveyance in the deed. Such a deed conveys to the new owner all the rights which the grantor possesses, but does not protect him against any adverse claim by other persons. A quitclaim deed, however, is just as effective to convey title to the land as is a warranty deed, and that is why the vendor's contract is performed by the delivery or tender of such a deed instead of a deed of warranty when the contract is silent as to the kind of deed to be delivered.

On the other hand the purchaser may reject the title as defective for any defect in the title which makes it unmarketable in cases where the contract calls for a quitclaim deed in the same way as where it calls for a warranty deed. The vendor must tender a deed conveying a title free and clear of encumbrances, whether it be the one or the other.

5. *Different parts of a deed.*—The opening part of a deed is called the premises. This recites the names and addresses of the grantor and grantee. Mistakes in spelling, initials, and the like, in the names do not invalidate the deed, provided there is enough to identify the parties with reasonable certainty. Then follows the granting clause, "does grant and convey," etc. A deed of release, used in releasing an adverse claim, such as a right of dower or other encumbrance, or an adverse title claimed by the man executing the

deed, contains the expression "grant and release." Next follow the description by "metes and bounds," beginning at a point fixed in some physical way, and describing the outer lines of the land by courses and distances around the parcel conveyed back to the point or place of beginning.

In construing the description, if an ambiguity arises because of a discrepancy between monuments and courses and distances, the physical monuments or marks control; the description of courses and distances will have to give way and be modified so as to make them conform with fixed physical objects referred to in the description, such for instance, as streets, a corner of two streets, a wall, a tree, a stream or other body of water, or a stone monument specially placed for the purpose.

After the description comes the *habendum* and *tenendum* clause, "to have and to hold," etc. This merely confirms the granting clause, and its object is to define exactly the estate or interest transferred. In case of apparent discrepancy they will be construed together if possible so as to give effect to both. If that is impossible because of the character of the discrepancy, it is generally held that the granting clause controls, altho that rule is subject to the rule of construction that the deed must be construed most strongly against the grantor and in favor of the grantee where an ambiguity or inconsistency exists.

6. *Covenants of title*.—In a warranty deed the usual covenants of title are six:

(a) Covenant of seisin, i. e., that the grantor is seised or possessed of the property as owner

(b) Covenant that the grantor has a valid right to convey it

(c) Covenant of quiet enjoyment, i. e., that the grantee will not be actually ousted from the whole or any part of the premises as the result of the wrongful acts of the grantor, or by any failure of his title

(d) Covenant against encumbrances, that there is no encumbrance upon the land other than those to which the deed has been expressly made subject

(e) A general warranty of title

(f) Covenant of further assurance, i. e., that the grantor will execute any further instrument of title that may be found necessary in order to convey a perfect title.

These covenants run with the land so that they can be enforced against the grantor by any subsequent owner taking title thru the grantee. The covenants of seisin, right to convey, and against encumbrances warrant a present situation of fact as being true and, therefore, if broken at all, they are broken as soon as made. The other three covenants are actionable only after the defect in the title has been enforced, or the owner has been ousted. As a practical matter that is true of the first three, since the enforcement of the encumbrance or the ousting of the owner must be proved in order to prove substantial damages.

7. *Mortgages*.—A mortgage is in the form of a deed conveying the property to the mortgagee as security for the loan or other debt due him from the mortgagor. The modern law treats the mortgagor as owner of the property in spite of the form of the

mortgage as a deed of conveyance. It holds that the mortgagee has a lien on the property to secure payment of the mortgage debt, which goes with the debt as an incident of it, and therefore the interest of the mortgagee is personal property, and passes as such on his death to his executor or administrator.

Payment of the mortgage debt destroys the lien of the mortgagee. On paying off the mortgage the mortgagor may demand a satisfaction piece which is filed in the public office where the mortgage is recorded, either the Register's or County Clerk's, and the mortgage is then satisfied of record. A tender of the amount due, which is not accepted by the mortgagee, has the same effect on the mortgage as actual payment, and may be set up as a bar to an action to foreclose the mortgage. However, the tender must be kept good by depositing the money in court as a condition precedent to having the mortgage canceled of record because of the tender.

If default is made in paying the mortgage debt when it falls due the remedy of the mortgagee is to foreclose the mortgage, and have the property sold under foreclosure and the proceeds applied to the payment of the mortgage debt.

In Massachusetts and several of the New England states the mortgagee is treated as the owner of the mortgaged land, and after default by the mortgagor, he is permitted to recover possession from the mortgagor and to hold the property until the mortgage debt is paid. In such cases he is called a mortgagee

in possession, and as such, he is compelled to account for all income derived from the land after deducting all necessary charges in caring for the property, including taxes, cost of necessary repairs, cost of insurance, and other necessary expenses incident to the carrying of the property, generally called carrying charges.

In New York and most of the states the mortgagee has no right to possession. But if the mortgagor surrenders possession to him, or consents to his possession, expressly or impliedly, the land is regarded as pledged as additional security, so that the mortgagee can hold possession until the mortgage debt is paid in full. To recover possession in such cases the mortgagor must bring an action to redeem, tendering or offering to pay the amount due on the mortgage. This action involves an accounting, in which the mortgagee in possession must account for all income received by him from the property. He is credited, as stated above, with all necessary expenditures of carrying the property, including taxes, necessary repairs, insurance, and the like. If the property, involved is rental property, the mortgagee is liable for negligence in failing to secure tenants; but if he has made reasonable efforts to find a tenant or tenants, he will not be charged with the rental value in case the property is not rented. If he has occupied the property himself he is charged with its fair rental value.

8. *Improvements by mortgagee.*—Tho the mort-

gagee is allowed for what he has laid out in making necessary repairs, he cannot recover anything for improvements made by him unless such improvements were made at the express or implied request of the mortgagor. He cannot, as the courts have put it, "improve the mortgagor out of his equity of redemption." If this were not the rule, the mortgagee might make it practically impossible for the mortgagor to get his property back by expending such sums for improvements that the mortgagor could never secure enough money to pay off the mortgage debt, plus the cost of such improvements, and his property would be lost to him.

9. *Rights and obligations of mortgagor.*—The mortgagor has the right to possession in all states until default on his part in paying the mortgage debt, and in New York and most of the other states his right of possession continues until the land has been sold and conveyed under foreclosure. By paying the mortgage debt on the day due he performs the conditions of the mortgage, and the latter is then automatically discharged.

A tender on the due day, not accepted by the mortgagee, constitutes performance of the condition by the mortgagor and, therefore, the mortgage is discharged and cannot be foreclosed thereafter. While the tender bars any action on the mortgage, yet the debt continues, and the mortgagor remains liable to a personal action on the debt. Nevertheless, as a practical matter, the mortgagee still has a very con-

siderable measure of security because the mortgage continues on the records as a lien against the land, and in order to clear his title so that he can sell the land free of the mortgage, the mortgagor must bring an action to cancel the mortgage of record. To maintain this action he must tender in court the amount due on the mortgage as tendered by him, and this is turned over to the mortgagee when the mortgage is canceled of record.

10. *Equitable mortgages*.—If a loan is made, relying on a promise by the borrower to execute a mortgage on his property as security for the loan, the property is held to be security for the loan in equity, tho no mortgage is in fact made. It is only fair that the lender should have the security promised to him on the strength of which he made the loan. Even tho there is no agreement in terms to make a mortgage in these cases, if the loan is made in reliance upon an agreement that certain property of the borrower shall be security therefor, a so-called equitable mortgage arises.

A common class of equitable mortgages comprises transactions in which a loan is made, the lender taking a deed, either absolute on its face or with a provision for repurchase by the grantor, the intent being to secure repayment of the loan by the deed conveying title to the property to the lender. Tho the instrument is a deed, not a mortgage, equity deals with it as a mortgage, securing payment of the loan according to the real intention of the parties. In these

cases the question is, did the parties intend the transaction to be considered as a loan or as purchase money for the property conveyed? If the former, the transaction is a mortgage, not a sale.

In all these cases of equitable mortgages, the mortgage is not enforceable against a purchaser of the property involved who has paid value for it without notice of the equitable mortgage. These mortgages are mere equities which cannot be enforced against subsequent purchasers of the property for value and without notice.

11. *Illegal mortgages*.—If the consideration of the mortgage is illegal, as when the mortgage debt arises out of any transaction involving the commission of a crime, or when the debt is tainted with usury, the mortgage cannot be enforced and is made void by establishing such defense. The usual case of this kind is a usurious mortgage. If any part of the indebtedness is usurious, the entire mortgage is made void, and cannot be enforced even as to items of the indebtedness not affected by usury. Of course, such valid parts of the debt may be enforced by personal action, but not by foreclosure of the mortgage.

But here, as in cases of tender, the position of the mortgagee is not so bad as might be supposed. The mortgage continues as a matter of record, and in order to get his title clear, the mortgagor must bring an action to have the mortgage canceled of record. This action is one in equity, and equity will refuse to give him relief unless he does what fairness and jus-

tice demands. Therefore, he must tender into court the amount received by him from the usurious lender in order to have the record cleared by canceling the mortgage of record.

In some states it is provided by statute that the borrower may have the mortgage canceled without returning anything. The courts have restricted these statutes to the precise limits of their provisions. Therefore the statute does not apply if the heir or devisee or trustee in bankruptcy of the borrower brings the action to have the mortgage canceled. The action is not brought by the borrower. In one case where the borrower got title back from his trustee in bankruptcy, the court held that he would have to return the money advanced by the lender, since he was not the borrower in the sense of the statute, holding by a title derived from such trustee.

12. *Assumption of mortgage by purchaser of mortgaged property.*—When the mortgagor sells the mortgaged property he must sell it subject to the mortgage, and the amount of the mortgage is deducted from the purchase price when the conveyance is closed and payment made. If the deed expressly provides that the grantee “assumes” a promise to pay the mortgage or the mortgage debt, the grantee becomes obligated to pay the mortgage indebtedness to the mortgagee. This is one of the most usual cases of a promise made for the benefit of a third person as beneficiary, discussed in a preceding chapter. It must appear that the grantor owes the debt

to the mortgagee. If he has taken title to the property subject to the mortgage without assuming it, he owes nothing personally to the mortgagee, and has no business securing an assumption of the mortgage from his grantee, and his grantee's assumption of the mortgage is void as a mere gratuity. It must appear, also, that the promise to pay the mortgage was for the benefit of the mortgagee, in the sense that it was intended to be enforceable by him.

In all the usual cases this is evident, but in a case of a deed of conveyance, given as security of a debt, and therefore really a mortgage, an assumption of an existing mortgage by this second mortgagee is merely a promise to take over the mortgage or to loan the money to pay it off, solely for the benefit of the mortgagor, and not intended to be enforced by the first mortgagee.

A very important practical matter to remember in these cases is that the liability of the original mortgagor on the bond, after the mortgage has been assumed by a grantee of the property, becomes that of a surety, so that an extension of the mortgage given by the mortgagee to the purchaser who has assumed the mortgage without the consent of the original mortgagor discharges such mortgagor from all liability on the bond, on the principle, previously explained, that an extension of time to the debtor discharges the surety unless the surety consented to the extension.

13. *Foreclosure of mortgages.*—The mortgagee may start the action of foreclosure the next day after the mortgagor has defaulted in paying the mortgage debt. Mortgages usually provide that if any instalment of interest is not paid within thirty days, or an assessment within sixty days from the time it is due, the mortgagee may declare the entire mortgage indebtedness due forthwith. In that case, after giving the required notice, the mortgagee may foreclose, tho the period for which the mortgage was to run has not yet expired. Often the same provision is inserted in case of failure to keep buildings on the mortgaged premises insured.

The necessary parties defendant in the foreclosure action include the mortgagor and any grantee, tenant, second or subsequent mortgagee or other lienor of the mortgagor and any other person having any interest in the property derived from the mortgagor after the mortgage become a lien on the property. The wives of any owners having a dower right in the property must also be made parties.

The result of joining all these persons is to foreclose or shut off their rights or interests in the property. If any such persons are not joined as defendants their rights are not foreclosed and still continue, so that the purchaser on the foreclosure sale may reject the title as defective, and the action will have to be brought again in order to enforce the mortgage.

Persons having an interest in the property, superior

or prior to the mortgage, cannot be made parties, since their interests cannot be affected by the foreclosure sale. Therefore, a tenant, a mortgagee, a creditor or other lienor whose interest is prior to the mortgage under foreclosure, having arisen earlier, cannot be made parties, and if joined and served, they may move at once to have the action dismissed as to them with costs.

The statutory costs allowed the plaintiff in the usual action of foreclosure amounts to a sum usually sufficient to compensate the attorney employed by the mortgagee to carry thru the foreclosure, so that the mortgagee usually loses nothing in legal fees when compelled to foreclose a mortgage. He or his representative will usually bid the property up to an amount equal to principal, interest and costs, so as to assure a sale price on the property to pay the entire amount due under the mortgage. The judgment entered in the foreclosure fixing the amount due and ordering the sale includes such principal, interest and costs.

REVIEW

Distinguish between real and personal property and discuss in this connection also the law of fixtures.

Describe a deed, and enumerate the usual covenants in a warranty deed.

Define the right of mortgagee upon default by mortgagor in Massachusetts and in New York.

State the ruling of the courts regarding the amount of repairs to be made by a mortgagee when in possession of premises thru default.

Explain the status of the parties where tender is made on the due day by the mortgagor and not accepted.

Define equitable mortgage, illegal mortgage. Discuss the position of the mortgagee in an usurious mortgage.

State who should be made parties in a foreclosure and why.

CHAPTER XXI

REAL PROPERTY—LEASES

1. *Landlord and tenant.*—Of greater interest to the business man than the matters of deeds and mortgages discussed in the preceding chapter are leases, which create the relation between landlord and tenant. A lease is a matter very commonly understood but in the language of the law it might be defined as a present transfer of an estate in land to the tenant. The usual case is a tenancy for a fixed term of years. The Statute of Frauds requires a writing to create a lease or a tenancy of over three years. In the Statutes of New York and many of the other states the period has been reduced to any tenancy of over a year. It must be signed by the grantor or his agent. In some states the agent signing must be authorized in writing. A parol lease for a year to start sometime in the future is good under that provision of the Statute which requires contracts not to be performed within a year to be in writing. A lease is a present transfer of an estate in the land to the tenant. A lease is performed as soon as made on the landlord's side, and of course, the rent may be paid and the contract performed within a year on the tenant's side tho the term of the lease is longer.

It is fundamental that ownership of the property with absolute control, subject to such limitations thereon as may be expressly provided for in the lease, shall be given to the tenant; otherwise the relation of landlord and tenant does not arise. If a right of enjoyment and use of the property is given to another without this ultimate power of control, the second party is a licensee, not a tenant. A licensee has no interest or estate in the land. He has a mere permission to enter and use the property in some definitely specified way or ways, but with possession and ultimate control remaining in the owner. For instance, occupation of land by a builder or other contractor in performing a contract to improve the property, the occupation of a room by a servant, the use of living quarters by a chauffeur, gardener, or janitor of an apartment as an incident of the employment, are instances of licenses, not tenancies.

Yet a servant may be a tenant whether he pays rent in money or in service, if it appears that the parties so intend. This will be true in all cases in which occupation of the living quarters are not convenient for and incident to performance of the contract of service, or when other circumstances show that the services are intended to be rendered and received as rent.

Boarders and roomers in boarding houses and hotels are merely licensees, since, in such cases, no intent to transfer an estate in the property can easily be inferred. However, the usual inference may be over-

thrown, and a tenancy held to exist when a lease in due form for a term is made for defined living quarters, tho board and service are also to be given by the landlord. This, at least, is the view in New York, and is probably the prevailing view, tho cases in Massachusetts and some other states hold just the opposite.

2. *Tenancies from year to year and from month to month.*—A tenant who holds over at the end of his term becomes a tenant from year to year if rent under his former lease was stipulated by the year, whether or not payable in monthly instalments, provided the landlord elects to permit him to stay on. If the rent is stipulated by the month he becomes a tenant from month to month. The landlord may elect to treat him as a trespasser and eject him from the premises. Acceptance of rent, or any similar act recognizing him as tenant, after he holds over binds the landlord to the tenancy from year to year or from month to month.

Notice of at least six months given by either one to the other is necessary in most states to end a tenancy from year to year and of at least one month to end a tenancy from month to month, and the notice must specify the end of one of the succeeding periods as the time when the tenancy is to end. It cannot be ended at any time during the year or during the month, as the case may be, but only at the end thereof.

The same sort of tenancy arises if the lease expressly provides for a tenancy from month to month

or from year to year. So also, if the lease is for no definite period, nothing being said in it as to its termination, but rent is stipulated by the year or by the month, the same rules as to notice apply.

In New York and many of the states the above common law rules have been modified, in New York, by decisions, and in Massachusetts and other states, by statute. Thus in New York, a tenant holding over is regarded as a tenant for another year or month certain at the landlord's election, so that tenant or landlord may end the tenancy at the end of the year or month without notice, and the same result follows each year or month if the tenant continues to hold over.

Tho tenancies from year to year and from month to month by express agreement are recognized, and the common law notice must be given, the New York courts hold that a tenancy at a monthly or yearly rental, nothing being said as to the duration of the tenancy, is a tenancy for one year or one month certain, renewed by holding over for another year or month certain at the landlord's election, requiring no notice to end it at the end of any one of the successive periods. A statute, applying to New York City only, makes five days notice from landlord to tenant necessary in order that a monthly tenant of this kind be dispossessed at the end of any month.

In Massachusetts all these tenancies are expressly made tenancies at will by statute, and may be terminated only by giving three month's notice. The

statutory provisions of the different states governing these tenancies vary greatly and must be consulted in each case.

3. *Tenancies at will*.—When no rent is stipulated by the year, month or week or when the tenancy is expressly at the will of either party, a tenancy at will arises. It may be ended by either party without notice at common law. In many of the states a notice from the landlord to the tenant is required to terminate the tenancy, varying in length from thirty days in New York to three months in Massachusetts.

A tenancy at will depends on the mutuality of the wills of the two parties; it is, therefore, personal and cannot be assigned. A conveyance of the property by the landlord or an attempted assignment by the tenant, therefore, ends the tenancy. It is also ended; for the same reason, by the death of either party. The statutory notice provided for in many states does not affect these rules.

4. *Tenancies under a void parol lease*.—A tenant entering under a parol lease for a term which requires a writing under the Statute of Frauds becomes a tenant from year to year or from month to month, depending upon whether rent under the void lease is stipulated on a yearly or monthly basis. The landlord must have recognized the tenant as such by accepting the rent or by some similar act recognizing the tenant as holding pursuant to the terms of the void lease. The terms of the void lease are implied as terms of the indefinite letting thus arising, and the

same requisites of notice apply as in the other cases, i. e., six months and one month respectively. But when the term of the void lease has run, no notice is required. The void lease is carried over so completely into the implied letting by the year or month that at the end of that period the implied tenancy ends without notice.

5. *Covenants in leases*.—Express covenants in leases speak for themselves and are construed and applied in accordance with the general principles of contract. The law implies a covenant of quiet enjoyment by landlord to tenant. This is broken if the tenant is ousted by the wrongful act of the landlord, or by his failure of title. Mere trespass by the landlord not resulting in the tenant's ouster is not a breach; the tenant has his remedy in trespass.

If the tenant is ousted as the result of the foreclosure of a mortgage which was a lien on the property before the lease was made, the landlord is liable for breach of the implied covenant. He is also liable if the tenant is ousted because of a nuisance maintained by the landlord in adjoining property, if it appears that the tenant was reasonably justified in quitting the premises because of the nuisance. In every case in which the tenant can sue for breach of the implied covenant he can set up eviction as a bar to an action for the rent. The rent is suspended by a wrongful eviction.

The tenant is no longer chargeable with rent when he is deprived of the land out of which the rent issues

by the landlord's wrongful eviction or failure of title. A wilful partial eviction bars recovery of the entire rent, but a partial eviction by failure of title results in an apportionment of the rent fairly covering that part of the premises which the tenant retains. He may, of course, rescind the entire lease in such case, but if he stays in possession of the remaining part, he must pay the *pro rata* rent in such cases in which failure of the landlord's title caused the eviction.

The implied covenant to repair which binds a tenant in favor of the landlord is merely putting in the form of contract the duty imposed on tenants from a very early time not to be guilty of permissive waste.

6. *Waste*.—Permanent damage to real property committed by a tenant for years or for life is known as waste. Destruction of buildings or other improvements, cutting of timber or other trees for the purpose of sale, failing to repair buildings or fences on the property or failing to keep ditches in repair, wasting the land by bad farming, reducing the fertility of the soil, opening new mines and working them, thereby permanently reducing the value of the property, are the more usual acts of commission or wilful waste.

Permissive waste arises from failure to make reasonable repairs causing the property to deteriorate in value. The tenant must keep the premises reasonably wind and water tight, keep plumbing in order and make such other repairs as are necessary to prevent permanent damage. He must paint when

needed to prevent deterioration and decay of the wood, tho not for ornament. He is not compelled to rebuild the whole or a substantial part of a building destroyed or damaged by fire or the like, or greatly deteriorated in spite of reasonable repairs.

7. *Surrender of leases.*—An express surrender of his lease by tenant to landlord must be in writing under the Statute of Frauds. A surrender by act and operation of law occurs in any case in which the tenant actually gives up the premises and the landlord accepts possession. If the landlord accepts the keys but notifies the tenant that he does so merely to care for the property on behalf of the tenant, and declares that no acceptance of a surrender will be made, the tenant remains liable on the lease. Generally, the landlord may in such a case relet the premises for what he can get and hold the tenant for the difference.

In New York, however, the landlord must show, not only that he notified the tenant that he would so relet, but the tenant must be shown to have received it and to have expressly or impliedly acquiesced. A clause in the usual lease to-day covers this by providing that the landlord may relet in such case, the tenant agreeing to pay this difference. The importance of this is that if a surrender occurs, as under the New York rule, rent is extinguished and the defaulting tenant is discharged, but under this provision he is bound to pay the difference by his contract. It is damages, not rent, and is not affected by the surrender.

REVIEW

Explain the legal nature of a lease and distinguish it from a license.

What is the status of tenants holding over after their leases have expired?

Explain tenancies at will.

Describe the usual covenants in the lease and those which are implied in it.

Give the rules of law governing the surrender of leases.

CHAPTER XXII

PERSONAL PROPERTY

1. *Aspects of personal property.*—Since the law of personal property has been treated in part heretofore in the chapters on sales and bailments, this chapter will cover only the law relating to chattels which have not been previously discussed. Such subjects as the rights of a mere possessor without other evidence of ownership, of a finder of lost property, of a bailee as against strangers, of an adverse possessor, will be considered first. Next we will discuss the methods of transferring title to chattels other than by sale, ending the chapter with a treatment of liens as they apply to chattels.

2. *Possession and ownership.*—Possession of property, real or personal, is ownership. From the earliest beginnings of our law the principle has always been recognized that the possessor must be protected as owner against every person other than the true owner. In the great majority of cases the possessor is owner, and giving him the right to protect and recover his possession as against a wrongdoer interfering with him is the best means of protecting his ownership, without subjecting him to the necessity of proving how he acquired his title. In the comparatively

few cases in which the plaintiff in such an action is a mere possessor, title being in another, the law will protect his possession against a taking of the goods by any person other than the true owner, because a refusal to do so would be an invitation to all others to help themselves to the goods by force. In that case any chattels or land which might happen to get into the possession of any person not the owner would be put outside the protection of the law, and would be held by mere force, resulting in a condition of anarchy in property control impossible under any system of law. This fundamental principle is illustrated in the particular cases here discussed.

3. *Lost property*.—The finder of lost property is owner as against every one except the true owner. This follows simply and solely from the fact of his possession. The finder must make reasonable efforts to find the true owner; if he knows who the true owner is, or could find out on reasonable inquiry, yet keeps the chattel for himself, he is guilty of larceny.

If the true owner appears at any time and demands the chattel the finder must restore it to him. But no one else can assert any right to the chattel. Thus if the finder loses the chattel shortly after finding it, he can recover it from another person who subsequently finds it. This follows from his previous possession which gave him title and ownership as against all persons other than the true owner.

4. *Lost chattels found on land privately owned*.—The weight of authority favors the rule that any chat-

tel found in a house, or on land not open to the public, belongs to the owner of the land, not to the finder. The owner of the land acquires possession of the chattel thru his possession of the land before it was found, and this possession gives him ownership ahead of the possession which the finder acquires.

In Massachusetts the owner of the shore was held in one case to be entitled to a stick of timber thrown up by the sea as against a stranger who found it there; also in England, the owner of a pool was held to be the owner of rings found in the bottom of the pool by workmen engaged in cleaning out the pool.

On the other hand the same principle has not been applied to lost objects found in safes, desks, bureaus, etc. The finder is held to be entitled to them in spite of the earlier possession of the safe or other article of furniture in which the lost object was found. It is clear that these two classes of cases are inconsistent. The first class of cases is the more reasonable since possession exists in the owner of the property where the lost article is found, whether he knew it or not, as power of dominion and control is in him, and this earlier possession should give him ownership against the subsequent finder.

5. *Misplaced chattels*.—Objects voluntarily placed on tables, counters or similar places and left there by mistake are not regarded as lost property. The law treats them as left in the custody of the owner of the place where they are abandoned, so that his earlier

possession gives him ownership as against the subsequent finder.

When, however, the chattel is found on the floor of a public place, as a store, railroad station, car, or the like, it belongs to the finder. Yet the finder should in such cases turn it over to the owner of the place where it was found so that it may be returned to the owner if he appears to claim it. If after a reasonable time the owner does not appear, the lost article must then be given back to the finder.

Likewise, chattels found in the streets may be turned over to the police, subject to recovery by the finder, if after a reasonable time the owner does not appear.

6. *Possession of tenant and bailee.*—A tenant of real property holding for life or for years is owner for the time being, and may recover the land from any person, including the landlord. At common law he was liable to the landlord for any permanent damages committed by a stranger even tho he was guilty of no negligence or other wrong and, therefore, he could hold the stranger for permanent damages to the land as well as for temporary damage to his interest for life or for years. It is well settled that a bailee, or holder, may recover the full value of the goods held by him as bailee which have been wrongfully taken by a stranger, the reason being that his possession gives him ownership as against third persons.

Following this principle, it is still quite generally

held, as in New York, that a tenant for years may recover for permanent damage done to the land by a stranger altho the ancient reason for the rule, i. e., his liability to the landlord in waste for such damage, is no longer recognized. In several states, however, it is now held that in case of permanent damage committed by a stranger, the tenant can recover only the damage which he has sustained as tenant, while the landlord alone can recover for the permanent damage committed by the wrongdoers. This very reasonable development in the law is likely to be generally accepted as law everywhere.

The same principle, however, has not been applied to bailments. The old rule that the bailee may recover the entire damages, subject to the duty of accounting to the bailor for his share of the recovery, is still law everywhere. Sooner or later, however, this probably will be modified, as the bailee's share or interest in the recovery is always comparatively small. It is apparent that a rule which binds the bailor by a suit, brought and prosecuted by the bailee without notice to the bailor, and without an opportunity on his part to be heard or represented by counsel, tho his share of the recovery is always greater than ninety per cent., is unreasonable and unjust. Of course, the bailor may sue the wrongdoer, but a judgment in favor of the bailee is a bar to his action.

In other cases of possession by an adverse possessor, (viz., one who wrongfully holds another's goods where no tenancy, license or bailment is involved) the

general principle that possession is ownership as against wrongdoers always prevails, so that full damages may always be recovered by the adverse possessor. The rights of the real owner are superior to those of the adverse possessor in such cases and he can proceed against either.

7. *Adverse possession*.—Possession of another's chattels for six years gives the adverse possessor ownership against the true owner because after that period the true owner's right to recover possession is barred by the Statute of Limitations. He must sue to recover the goods or their value within six years of the wrongful taking or his right to recover the goods is forever barred and his ownership is ended. The adverse possessor's ownership, good from the beginning as ownership against third persons, becomes complete ownership against the former owner as well.

It does not matter how often during this period the goods may be transferred from one adverse holder to another. The successive adverse holdings are joined or tacked together in order to make up the six year period, provided the adverse holders take possession from one another without a break. The period of the Statute of Limitations upon the action to recover the chattel or its value varies somewhat, it being five years in some states, tho in most states six years.

8. *Accession*.—The general rule is that the owner may follow his property and recover it within the period of the Statute of Limitations, no matter how

many times it may have been transferred. An important exception arises under the doctrine of accession.

Where raw materials are taken by a wrongdoer and manufactured into a finished product the owner of the raw material cannot recover the finished product, but is limited to an action for the value of his raw material where the increase in value due to manufacture is so great that it would be clearly unjust to permit a recovery of the finished product or its value. Thus the manufacture of lumber into pianos or violins, trees into finished building material worth several times the value of the trees, grapes into wine, wheat into flour, olives into oil, wool into clothing, etc., result in a transfer of title to the wrongdoer, leaving the owner an action for damages against the wrongdoer for the value of the raw material taken. That this rule shall apply, there must be a very considerable disparity in value, always several times the original value, tho no fixed rule on this point exists.

The old rule of Blackstone that there must be a change in kind, as wheat into flour, grapes into wine, no longer is recognized. The same wood or metal may exist in the finished product without change other than in form; the cases of most frequent occurrence in which the rule is applied in modern times are of this kind.

9. *Confusion*.—Another similar case of the transfer of title to personal property not arising out of the intent of the parties exists in cases of wrongful con-

fusion of goods. If a wrongdoer wilfully and fraudulently intermingles property of another with his own, where the units are of different value, the entire mass may be recovered by the innocent party, title to the wrongdoer's part passing to the innocent party because of the wrongful mingling.

Actual cases of transfer of title from this cause are rare, as in cases of most commodities the units are equal in value, so that each is owner of his share of the mingled mass in bushels, pounds or tons, and each may help himself to his part by measuring or weighing out the required quantity. In such cases no harm is done and the doctrine has no application. So in cases where the units may differ in value, and are such that they cannot be identified, as bales of cotton, sheep or other cattle, full justice may be done by letting the innocent party have his choice of his number of units, resolving every doubt in his favor.

10. *Voluntary transfer of title to chattels.*—All transfers of chattels for a consideration are sales and are dealt with in another chapter. Gifts of chattels require physical transfer of possession except in cases of deeds of gift in writing and under seal. A parol gift without delivery of possession is void as a mere promise to deliver not supported by a valuable consideration.

11. *Common law liens on chattels.*—From very early times a common carrier has had a lien on the goods carried as security for its charges, and an inn-keeper has had a similar lien on the baggage and other

personal effects of a guest brought on the premises by him. These benefits were undoubtedly given as a kind of offset for the duty imposed upon them to serve the public generally, whoever might apply, and for the extraordinary liability imposed on them making them, in effect, insurers of the goods and belongings of their customers or guests.

These liens existed in favor of innkeepers, tho the goods brought on the premises belonged to another, in fact even where the guest had stolen the goods. There is some authority for the same rule in the case of common carriers, but by modern cases and under modern statutes it is now generally settled law that the carrier has no lien on goods belonging to a stranger who had nothing to do with shipping them, and that a hotel or innkeeper has no lien on baggage or goods brought on the premises by a guest if he knew or should have known that they belonged to someone else. Hotels of all kinds, including apartment hotels, boarding houses and lodging houses have been included by statute with innkeepers in the benefits of these liens.

12. *Artisans' liens and liens of warehousemen.*—An artisan who has added value to a chattel by his labor or by additional material, or both, has a lien on the finished product for his charges, and may retain possession of the chattel affected until he is paid. It was held at first that this principle did not apply to livery stable proprietors or pasturers of cattle, or to warehousemen, but it is now settled law, either by

decision or statute in each state, that liens for their charges exist in all these cases, as also in favor of garage proprietors for storage charges or for work done on automobiles.

13. *Incidents of common law liens.*—In all cases of liens at common law the lien arises as a separate thing in connection with each contract. The lien is lost when possession of the goods is surrendered, and does not arise again as to any further balance due against goods of the debtor which subsequently come into the possession of the lienor. The cost of keeping the goods cannot be charged against the owners in these cases because it is done by the lienor for his own benefit. Of course, in the case of a warehouseman or similar case of storage for an indefinite time, the cost of storage runs on until the charges are paid, since such charges come within the terms of the original contract.

Permitting the owner to take out his horse or automobile for use during the day, returning it at night, is not a surrender of possession involving loss of the lien. Possession remains in the lienor in such cases, the owner having custody only for the day.

14. *General or commercial liens.*—General or commercial liens developed as part of the customs of merchants or mercantile law, recognized and embodied into the common law by decisions of the courts. The most important case is that of a factor who has a lien for advances and commissions. Another lien is that of a bank upon deposits for balances due from a

depositor. The most important difference between these two types of liens is that a commercial lien exists for the general balance on account due the factor or bank from the customer, irrespective of whether the items of such account are connected with the particular goods in which the lien is claimed or not, while a common law lien is limited to an amount due on the same contract thru which the lienor has secured possession of the goods. Furthermore, common law liens originally could not be enforced by a sale of the goods; they were used to worry the debtor into payment by withholding the goods. This has been corrected by modern statutes and decisions, so that such liens may be enforced by sale, either under foreclosure or by power of sale.

Commercial liens, on the other hand, have always been enforceable by a sale of the goods without any affirmative power of sale. The factor may sell to satisfy his charges, after giving reasonable notice to the consignor, tho against the express directions of the consignor and for prices lower than those authorized by him.

REVIEW

State the rules as to ownership of personal property when found in a public street; on privately owned land; in a store.

Explain the rights of the real owner of property which has been converted into another form for purposes of sale.

In cases of confusion of personal property, tell what rules are followed in determining the rightful title.

Discuss liens on personal property from the standpoint of the rights of common carriers and hotel keepers.

Distinguish between commercial liens and common law liens.

CHAPTER XXIII

FIDUCIARIES

1. *Nature of the relation.*—It is part of the legal conception of ordinary trade that the parties deal with each other as it is said “at arm’s length.” Each is looking out for himself and seeking a profit. Neither is under any obligation to concern himself for the profit or protection of the other. But certain relationships exist where one party assumes an absolute legal obligation to disregard or eliminate his own pecuniary interest and to act in the matter solely in the interest and for the profit of another. This is called a fiduciary relationship or trust and may be defined as the obligation arising out of the confidence reposed in a person who holds some interest in or power affecting property of any kind for the benefit of another. The person holding the property or power is called the trustee; the person for whose benefit it is held is the beneficiary, or *cestui que trust*; the thing held is the trust fund, trust estate or *res*.

The fiduciary or trust relationship occurs in various transactions some of which are not technically trusts. Some of the more frequent trust relations are those of executors, administrators, guardians, agents, bailees, partners, directors of corporations, assignees for specific purposes. In fact a fiduciary relation-

ship arises whenever one person receives the money or property of another for a particular purpose.

To constitute a valid technical trust, three things are necessary: (a) a trustee, (b) another person who is the beneficiary, and (c) the property. Without each of these three, a trust cannot exist. Where the trust is created by the positive and direct acts of the parties in writing it is called an *express trust*. For example, Jones by written agreement transfers to the Loyalty Trust Company money or property to be held by it for the benefit of his son Henry. Jones may do this by will or by a transfer in his lifetime. If Jones adds a provision that such trust fund is not to be subject to the demands of any creditor of the son, it is called a *spendthrift trust*.

When the trust is not so created but when it can be seen from the words or acts of the parties that such a relationship was clearly intended, or when equitable principles clearly require the imposition of such obligation, even in the absence of such intention of the parties, in order to prevent fraud, we have an *implied trust*. For instance, if Jones should pay the purchase price of property which the seller then transferred not to Jones but to his brother or a friend, the transferee would get the legal title but would hold the property in trust for Jones without any express agreement on the part of the former. So if Jones, in order to conceal his identity, should furnish his friend the money to open and operate an account with a stock broker in the friend's name,

the friend would become a trustee and Jones, the cestui que trust. In each case the friend would have the legal ownership i. e. the title, while Jones would have what is called an equitable interest or equitable title, so-called because under the common law such an interest could be enforced or protected only by a court of equity as distinguished from a court of law.

2. *Trust property*.—Any property or right, real or personal, which can be assigned or transferred can be made the subject of a trust. Generally speaking, property rights can be assigned while strictly personal rights cannot. The right to receive payment of a debt or to collect damages for the conversion of or injury to property may be assigned but, for instance, the right to collect damages for slander or other injury to one's person, altho valuable, cannot be assigned. Hence they could not be held in trust.

Frequently property is held under a trust giving the income to one person and the property itself to another. In such cases puzzling questions arise as to what is income from the property as distinguished from the property itself, or using the usual technical terms, which is income and which is *corpus* of the trust estate. If a fund of \$50,000 is invested in bonds the interest received is income, but if the trustee should exchange the bonds for other bonds worth \$55,000 the resulting *increase* of \$5000 would be treated not as income but as an addition to the body or corpus of the trust estate. If the bonds depreciate in value in the hands of the trustee the interest is

still income and cannot be added to the corpus to make good the deficiency unless the provisions creating the trust expressly provide for it.

In the case of corporate stock held in trust, all cash dividends paid out of surplus earnings would be income. On the other hand, stock dividends have been the subject of conflicting decisions by the states and so the fiduciary must ascertain the prevailing view in each jurisdiction. In case of a sale and repurchase of capital stock or its exchange into other stock, the resulting profit would be corpus, not income. When a trustee of a mortgage forecloses, buys the property at the foreclosure sale and afterwards sells it at a profit, the resulting profit is regarded as an increase in corpus, not as income.

The trustee's accounts should be kept so as to show the exact nature of each item, whether it is a part of the income or the corpus of the trust property, whether it is a loss or an expense incident to the management of the trust. Any property rightfully or wrongfully substituted for the trust property is considered as such as long as it can be traced. If the fiduciary mingles the trust property with his own he violates his trust. If, because of such act, the trust property cannot be separated from his own, the whole will be treated as trust property, at least, so far as it is necessary to the full protection of the beneficiary. In connection with the subject of proper accounting by a fiduciary the reader should

refer to a good text because it is important that all transactions be handled properly.

3. *Rights and duties of trustee.*—The first duty of the person undertaking a fiduciary obligation in respect to property is to take possession of the trust property, or secure control, or notify obligors or custodians of the property of the interest which he has acquired. Diligence in this respect is usually necessary to protect the estate from loss. Especially in regard to the collection of debts, any delay which results in loss of any part of the debt is likely to be deemed negligent.

However, if a suit is necessary to collect a claim and the trustee employs an attorney thru whose delay the debt becomes uncollectible, the trustee would not be liable. The employment of an attorney is usual and necessary in such cases and the trustee must rely upon him.

The general duty of a trustee or fiduciary may be explained by saying that he is the legal owner of the trust property and has all the rights and obligations of the owner, *and more*. A personal confidence is reposed in him which calls for the highest good faith and reasonable diligence. It is not enough that he deal with the property as he would with his own.

He may, for example, intrust his own affairs to others but he may not delegate to another a duty which he owes to the beneficiary unless such delegation is the usual and necessary means of doing the

business, such as in employing an attorney to bring suit. Again, if his fiduciary obligation requires the investment of funds he may seek advice but he cannot delegate the duty of deciding what investments shall be made. He is bound to exercise ordinary skill and judgment. If he is not qualified, he should not accept the trust.

If several persons are co-trustees, as in the case of several executors, or a partnership, or a committee, they must act unanimously, for the judgment of all is requisite. If they cannot agree they cannot act, unless the provisions creating the trust provide or contemplate action by a majority. When partners are appointed agents by the firm name it is, of course, contemplated that they will act in such capacity as a partnership acts. Therefore, one partner could act in discharge of the fiduciary obligations.

Here it is necessary to distinguish between public and private trusts. A public trust is one established for the benefit of the public or for a considerable portion of it, such as trusts for religious or educational purposes, for hospitals, orphanages, etc. In such a trust, co-trustees are usually named and are authorized to act by a majority of the entire number who are qualified. One trustee is not responsible for the dishonesty or negligence of a co-trustee in the absence of connivance or bad faith. Nor is it negligent for one trustee to allow a co-trustee to retain possession of the trust property when there is no reason to suspect him of irregularity.

4. *Investments by trustees.*—The most important duty of a trustee is to carry out, faithfully and diligently, the terms of the trust or the instructions of the person creating the trust or reposing the confidence. It is hardly less important that he should invest the trust fund so that it shall, first of all, be safe and, secondly, yield a reasonable income, subject, of course, to instructions in the instrument or agreement giving rise to the trust. The trustee may not lend trust funds upon the personal security of anyone. Since a promissory note is simply evidence of a debt but not security for it, he could not loan on such an instrument.

On the other hand, he should not allow funds to lie in a bank for a long period when good investments are available. While he cannot, however, invest funds in trade or manufacturing, and in New York and Pennsylvania not even in the stocks of corporations engaged in trade or manufacturing or transportation, yet there are certain types of investments that are legal for such funds. Some states, in recognition of the investment status that the stocks of some corporations have attained, permit trustees to invest in bank stocks and the stocks of public utilities, and insurance corporations. It behooves the fiduciary to find out what investments are legal in his particular state. In general, however, various restrictions limit the trustee to first mortgages on real estate and government and municipal bonds.

If the trustee unreasonably delays the investment

of the trust fund he is personally liable for the interest lost. If he invests it improperly and it is lost, he is personally liable for the loss; but if his improper investment yields big returns, the beneficiary alone receives the profits. The trustee always bears the risks; the beneficiary receives the profits. This is to remove temptation from the trustee.

Of course, the agreement creating the trust may authorize investment in specific securities or enterprises. The beneficiary may, if he is an adult and competent, assent to or request a particular investment. In that event he cannot compel the fiduciary to bear the loss if the latter has acted in good faith.

5. *Other duties of a trustee.*—The trustee can make no profit for himself, directly or indirectly, except as agreed to in the trust agreement. In the absence of such agreement, he is entitled to reasonable compensation for his services. If the parties cannot agree upon the amount, the court will fix it upon his accounting. For necessary disbursements, the trustee may at any time reimburse himself out of trust funds in his hands.

It is the trustee's duty to keep full and intelligible accounts and to be prepared to render a full account supported by vouchers at all times. When the beneficiaries are competent adults the trustee should consult their wishes but not be controlled by them, unless such control is contemplated by the trust agreement. Thus the trustee for bondholders, since he is appointed only for convenience, must carry out the

wishes of the bondholders, while the trustee of a spendthrift trust would ordinarily not be controlled by his beneficiary since such trusts are usually created because of lack of confidence in the wisdom of the beneficiary.

An agent is obliged to obey most implicitly the instructions of his principal and departs from them at his peril, while a guardian of an infant's property must obtain the approval of the proper court for practically every payment made out of the trust property, regardless of the purpose or necessity for it.

6. *Relations of third persons to the trust.*—When a person holds property in trust or in a fiduciary relationship, a third party who deals with him concerning the trust property must take notice at his peril of the extent of the fiduciary's authority. If the third person receives such property with notice of the trust but in violation of its terms he is guilty, equally with the trustee, of a fraud upon the beneficiaries. This principle extends to all fiduciary relationships, regardless of whether they are technical trusts or not. A third person who receives firm property in payment of the debt of a partner, or who receives from the guardian of an infant any part of the trust estate not paid or delivered for an authorized purpose, becomes accountable to the co-partners or infant to the extent of the value received.

When a trustee or executor or other fiduciary deposits trust funds in a bank, the bank may become

accountable to the beneficiary if it knowingly honors checks drawn against the fund for unauthorized purposes. Hence it is the common practice for banks receiving such deposits to require the filing with them of copies of the trust agreement or court order under which the fiduciary is acting.

When the fiduciary is entitled to receive the proceeds of property sold by him for a specified purpose only, for example, to divide it between two named beneficiaries, the old English law went so far as to say that the person buying the property and paying over the money must see that the money was applied to the purposes named. In the United States, however, the third person has been relieved generally from that obligation. But where one who owed money to an infant paid it to the infant's guardian before the guardian had filed the bond required for the faithful performance of his duties, and the guardian absconded, the debtor was required to make a second payment of the money to the new guardian.

If the transaction appears to be a valid exercise of the authority of the fiduciary, if there are no suspicious circumstances and the third person acts in good faith and gives full value for whatever he receives, the latter's rights are not questioned and his title will be protected by the courts, regardless of the fraudulent conduct of the fiduciary. Property subject to a fiduciary relationship will be traced and recovered as long as it or the proceeds of it can be traced, but only until they reach the hands of a bona

fide purchaser for value. To take them from such a holder and restore them to the beneficiary would be to commit one injustice in order to redress another. This, a court of equity will not do.

The creditors of the trustee or fiduciary individually cannot levy upon the trust property. Their only remedy is against his individual property. Those who have extended credit to him in such capacity or have rendered services to the trustee which have benefitted the trust estate must also in most states look to the trustee individually for payment. He becomes personally liable upon such contracts and may reimburse himself from the estate in a proper case. In some of the states, among them New York and Ohio, he can by express terms of the contract limit liability on the contract to the trust property.

7. *Rights of beneficiary.*—The beneficiary has the right to compel the trustee to carry out the terms of the trust. If there is reason to suppose that the trustee is about to act in violation of the confidence reposed in him, the beneficiary may secure an injunction restraining the trustee. The beneficiary is entitled to an accounting by the trustee as often as necessary for his protection. When the purposes of the trust have been accomplished the beneficiary has the right to compel the trustee to transfer the trust property to him.

If any of the trust property has come into the hands of a third party who is not a bona fide purchaser for value, the beneficiary may compel him to

make restitution or account for the property. In fact, if the trustee at any time fails to act with diligence in the collection of money or the enforcement of rights affecting the trust, the beneficiary may in his own name enforce his rights by proper legal proceedings against the third party. Even tho the legal title is in the trustee, the beneficiary is not confined to his action against the trustee for neglect. But before taking action against the third person, the beneficiary must demand such action by the trustee, the general rule being that actions should be brought by the person having the legal title to the right or property involved.

A familiar application of this principle of law is found in the case where a fraud or other wrong has been committed against a corporation. In the eyes of the law the corporation is the person injured and an action for redress can usually be begun by the corporation only, not by an officer or a stockholder. But if the directors and officers corruptly or negligently refuse, after demand made, to bring the proper action in the name of the corporation, one or more stockholders who have made such demand may begin the action in his or their own names on behalf of the corporation. The rule is equally applicable where the guardian of a minor neglects his duty, or where an auctioneer or other person in whose name a contract is made for the benefit of another fails to enforce the rights accruing under it.

REVIEW

Define fiduciary, cestui que trust, spendthrift trust, implied trust.

State why it is important to keep separate, corpus and income.

Outline the rights and duties of a trustee.

Discuss investment of trust funds by a trustee.

Describe the rights of a beneficiary and his relationship with the trustee.

CHAPTER XXIV

QUASI-CONTRACTUAL OBLIGATIONS

1. *Nature*.—The nature of quasi-contractual obligations will appear more clearly if the ground is first cleared by a brief survey of the situations which impose an obligation upon the individual.

(a) Certain wrongful acts are in their nature or effect so detrimental to public welfare that the law subjects the doer of such an act to fine or imprisonment. These acts are called *crimes*.

(b) Certain other wrongful acts also violate the rights of another to be allowed to possess and use his property and to pursue his business or pleasure free from wrongful interference, but may not impair public order or welfare seriously or at all. These wrongful acts are called *torts*. The more common are conversion of another's property, fraud, assault, slander, libel, seduction, malicious prosecution of another for crime, and the failure to use reasonable care not to injure another's person or property. These acts give to the person injured the right to recover compensation for the wrong by way of damages. An action brought for such purpose is a *tort action*. Sometimes the same act may be both a *tort* and a *crime*. For example, assault, libel and fraud may be

punished by the state as offenses seriously detrimental to the public peace and welfare, while at the same time the person suffering the particular injury may prosecute his action for damages. The wrongful appropriation to one's own use of the property of another is called conversion. When the property is so used because it is mistaken for one's own the taking or using of it is still a wrong, a *tort*, and gives the owner a right of action for damages against the person so taking or using the property. But if the taker of the property takes it stealthily, knowing it is not his own and intending to deprive the owner of the chattel, the taking constitutes not only the *tort* known as conversion, but also the *crime* of larceny. The owner may sue him for damages and the state, acting thru its prosecuting officers and courts, may imprison him for the crime. Both the civil action and the criminal prosecution may proceed at the same time.

(c) A third class of acts or omissions not in themselves wrongful may become wrongful because they are violations of an agreement to which the law gives validity. These are violations of contract. These have been discussed in the chapters on contract. Actions brought for the violation of contract obligations are called *actions on contract*.

In distinction from the cases above noted there is another class of wrongful acts or omissions which are not crimes, or torts, or violations of any contract, but which are violations of a duty to refund money

or make compensation for property or for a benefit received by one under such circumstances that for him to retain it without such compensation is regarded by the law as unfair, inequitable and a violation of the ties of natural justice. These wrongs are redressed by the same actions for damages that are employed for the redress of breaches of contract. Because of this similarity of remedies the obligation arising from such a wrong is called a *quasi-contractual obligation* or *quasi-contract*.

Yet the reader should not be misled by the name into thinking of these obligations as some sort of contract obligations. Since the wrongful act or omission is not a violation of any promise, expressed or implied, it is more like a tort than like the breach of a contract. Another important distinction is in the remedy. The commission of a tort and the violation of a contract are both redressed by an action to recover damages. In both cases, when it comes to fixing the amount of damages the offender must pay, the questions are always, How much was the *plaintiff damaged* by the wrong done? What amount will fairly compensate him for the injury done him by the offender's wrongful act or omission? But in the case of the wrongs now to be considered the inquiry is always, How much has the *defendant benefited*? What amount fairly represents the benefit that the defendant has received which in fairness and good conscience he ought not to retain? In short, instead of its being a survey of damage done to one party

it is a survey of benefits received by the other.

2. *When the obligation arises.*—Two elements are necessary to the existence of a quasi-contractual obligation:

(a) The defendant must have received a benefit from the plaintiff without giving compensation for it

(b) The circumstances must be such that it would be unfair and against good conscience for the defendant to retain the benefit without making compensation.

There are several situations where both these elements exist and yet the law imposes no obligation to make compensation. Before considering these exceptions let us consider a few applications of the rule.

3. *Mistake.*—Suppose that, in paying for goods, a customer by mistake hands a merchant a one-hundred-dollar bill instead of a ten-dollar bill. He has overpaid the merchant \$90. In other words the merchant has received a *benefit* of \$90 for which he has given the customer nothing. It is unjust and against good conscience for the merchant to retain the \$90. The law requires him to return it as soon as he discovers the mistake, regardless of whether the customer has demanded restitution or even discovered his mistake. It matters not if the customer was most careless in handling his money; such carelessness does not justify the merchant in enriching himself at the customer's expense. The same rule is applied when a man by mistake pays a bill twice, when an illiterate

man errs in computing a balance due and consequently overpays or when mistakes made in weighing or measuring goods result in overpayments for them. On the other hand, if the mistake results in underpayment, the seller can treat the amount paid as a part payment and sue for the balance *due under the terms of sale*. His action, therefore, would be the ordinary contract action for breach of the customer's promise to pay. There is no need to inquire into the fairness, or so-called equity, of the transaction.

Again, suppose the merchant, thru a misunderstanding, ships to the customer a carload of coal which the latter did not order but which, by mistake of the customer or his employes, is received and used before the mistake is discovered. Here there is no promise to pay for the coal; in fact, the coal may have been too valuable for the customer to use profitably in his operations. Yet it would be unfair for the customer who has used the coal to pay the merchant nothing for it. It might be equally unfair to the customer to compel him to pay the merchant the market value of the coal when coal of a different and cheaper grade would have served the customer's purpose equally well. The law, therefore, compels the customer to pay, not the market price of the coal, but the amount which the use of the coal has presumably saved the customer. Ordinarily, this would be the amount that the customer would have paid for other coal to do the same work.

4. *Mistake as to existence of a contract.*—It may

happen that services are rendered or goods delivered, supposedly pursuant to a contract when, because of a misunderstanding, no contract exists. In one case Turner offered to serve Webster as a watchman for "\$1.50 per day and nights the same," meaning \$3.00 for a day of 24 hours. Webster employed Turner but understood him to mean \$1.50 for 24 hours. Since the terms were ambiguous and neither man had understood the other, there was no contract of employment. But as it would be unjust for Webster to receive the benefit of Turner's services without making compensation, Webster was required to pay the reasonable value of the service received by him.

If Webster, however, had merely requested Turner to act as watchman and Turner had so acted, nothing being said about the price, their conduct would have indicated an intention to give and to receive the service at its reasonable value. A true contract then would have been made. But in the case mentioned above, the parties did not intend to render or receive the service at its reasonable value; they intended to agree upon a price but failed to do so. Hence their conduct in rendering and accepting the service did not amount to an actual contract. The law, however, imposed the obligation upon Webster in order to prevent injustice.

5. *Mistake as to identity of dealer.*—If one receives and uses goods, supposing them to have been delivered by one firm but finds later that they were

actually supplied by another, his acceptance and use of the goods amounts to a promise to pay *only the person who is supposed to have delivered them*. But as he has had the benefit derived from the use of the goods it would be ordinarily against good conscience for him to pay nothing for them. Accordingly, he must pay the firm who supplied the goods their fair value to him.

In a notable Massachusetts case Potter had been buying ice from the Boston Ice Company for use at his residence, the daily purchases being determined by orders given by his servants. He became dissatisfied with the service, terminated his contract, and made a new contract with the Citizens' Ice Company. Subsequently the Citizens' Ice Company sold out its business to the Boston Ice Company which company continued the delivery of ice to Potter who received and used it without notice of the change in the business. Potter refused to pay for the ice furnished by the Boston Ice Company after he had refused to deal with them and was sustained by the court. The decision was based upon the ground that the ice company, in thrusting itself upon Potter without notice, knowing that he did not wish to deal with it, had acted officiously and that, under the circumstances, it was not inequitable or against good conscience for Potter to refuse payment. Of course, he could not return the ice upon discovering the seller's identity. Yet had the subject of the transaction

been an article which still remained in Potter's hands it would, of course, have been his duty either to return the article or to pay its value.

6. *Mistake as to subject of a contract.*—Contracts of sale of specific articles are frequently made when the articles are not present at the place of sale. In such cases their existence is commonly assumed. If it happens that the article sold had perished before the sale, the contract of sale is void. If the purchase price has passed to the seller he must return the money, otherwise he would be unjustly enriched at the expense of the buyer.

Suppose, for instance, that Brown, believing he has goods at sea insures them and pays the premium, but in fact they had been lost before he made the insurance contract; the insurance contract is void. The insurance company is not liable for the loss but is liable for the return of the premium. This would not be the case, of course, if the company undertook to insure the actual *existence of the goods* as well as their future arrival at their destination.

Sometimes a mistake in the nature or identity of the thing sold will avoid the contract and entitle one of the parties to restitution. In a Michigan case a blooded cow was sold for \$80, both parties believing her barren. When it transpired that she was in fact with calf and worth nearly \$1000, the seller refused to deliver and rescinded the contract. The court upheld him upon the ground that a barren cow was a

substantially different creature from a breeding one and not in fact the animal or kind of animal that the parties had intended to buy and sell.

The case was a doubtful one, for the rule is that mistakes in kind or quality of a thing sold do not ordinarily give rise to an obligation of the lucky party to make restitution. For instance, Mrs. Doe finds among some keepsakes given her by her deceased aunt a small stone which she guesses to be an uncut topaz and sells it for \$5.00 to the local jeweler who shares her opinion as to its nature. It turns out to be an uncut diamond worth \$1000. If both Mrs. Doe and the jeweler were uncertain as to the nature of the stone, and both were consciously taking a chance as to its real value, it is not unjust or against conscience for the jeweler to retain the benefit of his bargain.

But if both supposed it to be a topaz and intended only to buy and sell a topaz the contract would be void because of the mistake as to the identity of the subject of it. In that case it would be clearly against conscience for the jeweler to retain without compensation an article which he did not expect to buy and which she did not intend to sell. Upon her offering to return the purchase price it would be his duty to return the stone or pay her its value.

7. *Mistake as to a material fact.*—Not every mistake leading to the payment of money will entitle the person so paying to demand its return. It must be an honest mistake as to a fact directly affecting the

legal liability to pay. Where a mortgagee, in order to protect his security, pays taxes or other claims which he mistakenly supposes are liens upon the property, and discovers his mistake, he cannot, recover his money for he was under no obligation or legal liability to pay the claims in any event.

Furthermore, if the one who pays is aware at the time that there is doubt as to a material fact and pays without full investigation or to avoid a controversy, he cannot recover the amount paid.

For illustration, Jarvis insured his life and then disappeared. Seven years later the beneficiary made claim upon the insurance company for payment under the policy. The company was uncertain whether Jarvis was alive or dead but to avoid litigation and, perhaps, the imputation that it resisted payment under its policies, it paid the amount of the policy. Later Jarvis was found to be alive. But the company could not recover the insurance paid. The payment was not made by mistake but by way of compromise. It is the policy of the law to discourage litigation and to make settlements of controversies by compromise final.

But where an insurance company paid the beneficiary under a life policy because the officers had forgotten the fact that before the death of the person insured the policy had lapsed for nonpayment of premiums, the company was permitted to recover the money paid. Whether the mistake arises from ignorance or forgetfulness is immaterial, provided

it is not a compromise and not made at a time when there is a doubt actually present in the mind.

8. *Mistake of law*.—Since it is every man's duty to ascertain the law before taking action, the law in most states will not aid him to recover money or property which he would not have paid or delivered but for his ignorance of the law. For instance, if Green's child mischievously procures goods from a merchant and consumes them, the merchant supposing the child was sent for them by Green, and the latter, in ignorance of the law that a parent is not liable for the wrongs done or mischiefs committed by his child, pays for the goods, he may not upon discovering his mistake as to the law, recover the money from the merchant.

9. *Other cases of retaining benefits without making compensation*.—There are many cases where, altho one has conferred a benefit upon another without consideration, the circumstances are such that to compel payment for such benefits would work one hardship in order to relieve another. The law will not do this. For instance, if Brown in paying money to an agent overpays by mistake and before the agent has notice of the error he turns it over to his principal, Brown must look to the principal for a recovery of the excess payment. It would be a hardship to compel the agent to reimburse Brown.

In one case Schirmer delivered to the railroad company rice consigned to Wilson who reported non-delivery and Schirmer claimed and received from

the railroad payment for the lost consignment. Subsequently after Wilson had gone out of business and disappeared, the railroad company upon discovering that the rice had been delivered to Wilson, sued Schirmer to recover the amount paid him by the company. But the court held that, inasmuch as Schirmer had lost his chance to recover the price of the rice from Wilson so that repayment by Schirmer would result, not in restoring the parties to the position they had previously occupied, but merely in shifting the loss from the company to Schirmer, it was not inequitable for Schirmer to retain the money.

Of course, if the original mistake had been caused solely by the negligence of Schirmer, he should have returned the money regardless of whether he could recover from Wilson or not. But where neither party is negligent, or where both are equally negligent, in connection with the original mistake the courts adhere to the rule illustrated by the above case.

Again suppose that a merchant in ignorance of the fact that the Statute of Limitations has run against a debt for money borrowed by him pays the uncollectable debt. Upon discovering that he need not have paid the money he cannot recover it. Altho the creditor could not have collected the debt, yet having received the money, it is not inequitable for him to retain it. The law creates no obligations to repay unless it would be unjust and contrary to good conscience to retain the money.

10. *Illegal contracts*.—Ordinarily, a contract which contemplates a violation of law by any party to it is void and unenforcible. If Green bribes Sharp to vote for a certain measure and pays him \$1000 in advance, Sharp may safely take the money and virtuously vote against the measure. Green cannot recover the \$1000 from Sharp for the courts will not suffer the indignity of being used to settle disputes between criminals. This rule is rigidly applied when the contemplated act is one involving moral delinquency. Such rule was applied where Sharp agreed to sell Green \$3000 in counterfeit money for \$300 of real money paid him by Green but did not perform his agreement and Green sued to recover the \$300.

When, however, the act is not grossly immoral, altho forbidden by law, the courts will often compel payment for benefits received under an illegal contract. Thus, to discourage gambling, the loser in most states may recover from the winner the money lost. A contractor who has agreed to erect a building after plans that call for construction which violates a city ordinance may erect that part which is legally permissible and recover from the owner the reasonable value of the work done while refusing to go on with the rest of the job. This is because the law encourages the withdrawal from an illegal contract before the illegal act has been performed. Had the contractor, however, erected any part of the work which violated the law he could not recover for any

part of the work done. The courts would regard both contractor and owner as wrongdoers equally guilty and would aid neither.

The defense that the plaintiff ought not to recover for benefits conferred upon the defendant because he is as much of a wrongdoer as the defendant will not prevail, however, where the plaintiff has been dominated by the defendant or belongs to a class that the law seeks to protect. For example, a failing debtor at the advice of his attorney conveys property to his attorney in order to defraud his creditors. Both are wrongdoers but the debtor has acted under the domination of the attorney. So, altho marriage brokerage contracts are forbidden by law, yet one who has paid another money to find him a wife is regarded as under a species of imposition or undue influence and, altho a wrongdoer, may recover the money paid. Again, since it is more important that agents shall be faithful than that employers shall not engage in illegal business, an agent cannot refuse to pay over to his principal, money which has come into the agent's hands in connection with an illegal transaction.

11. *Contracts void because of Statute of Frauds.*—In general, the various so-called statutes to prevent frauds and perjuries provide that no contract concerning an interest in land, or for the future sale of goods or chattels for over \$50, or for other acts not to be fully performed within one year, shall be valid or enforceable unless it is reduced to writing and signed

by the party to be charged or held liable upon it. When one has delivered property or rendered services to another under an oral contract, unenforcible because of the Statute of Frauds, the law regards it as unjust and inequitable for the other party to retain the benefit while taking advantage of the defense furnished by the Statute. The courts, therefore, while refusing to enforce the oral contract, will, nevertheless, compel the defendant to pay for the benefits received by him. In the case of goods sold or services rendered this amounts to a practical enforcement of the contract. The defendant will be compelled to pay the reasonable value of the goods or services, which is usually not far from the contract price.

But if the party who has partly performed his contract refuses to go on with it, and at the same time tries to exact payment for so much of the work as has been done from the other party who is willing to complete the contract, it is not deemed inequitable for the latter to retain the benefits and refuse to make payment unless and until the former completes his contract. The law does not discourage the performance of contracts which do not comply with the Statute of Frauds but are otherwise legal. In consequence one who has partly performed such a contract must go on and complete his contract or lose the right to compensation for the part performance. Assume, for example, that Brown makes an oral agreement to work for Sharp for two years at \$5000

a year. If, after he has worked six months, Sharp repudiates the agreement and discharges him, Brown can recover from Sharp the reasonable value of his six months' service. But if after six months Brown wishes to repudiate the agreement and quit the employment, he can recover nothing for the work done.

As has been said, the law compels the defendant in such cases to pay only for benefits received by him and not for damage suffered by the plaintiff thru his reliance upon the void contract. Suppose Sharp agrees verbally to pay Brown \$5000 for a machine to be furnished and built in accordance with drawings to be supplied by Sharp, and placed upon Sharp's premises. Brown furnishes the labor and materials and constructs the machine. At any time before the machine has actually come into Sharp's possession he may repudiate the contract with impunity. The contract not being in writing it cannot be enforced against Sharp. And since Sharp has not received any benefit he has not been enriched, justly or unjustly, at Brown's expense. Brown must bear the loss because he has been short sighted enough to rely upon a contract which did not comply with the Statute of Frauds.

12. *Benefits voluntarily conferred without contract.*—It would be most unfair to require one to pay for a thing which he has received only because it was given to him. The donee, therefore, is within his rights in refusing to pay for the gift. When two

neighbors, who have been accustomed to render each other neighborly services without charge, have a disagreement it is not inequitable for either one to refuse to make payment for such benefits as he has received in the past. Nor is it inequitable for an orphan who has received charitable support to refuse payment for it when he later comes into possession of property. In short, one cannot recover for services rendered or benefits conferred unless he expected at the time to be paid therefor. But if he intended at the time to claim compensation and if he was not acting officiously or intermeddling, he may ordinarily recover for the benefits conferred, unless they were such as commonly are rendered without compensation, as, for instance, emergency services in time of fire, flood or accident.

The law does not permit Smith to make himself the creditor of Doe by paying Doe's debts. Smith would be deemed an intermeddler and could not recover for the benefits thus officiously bestowed upon Doe. But if Doe borrowed Smith's automobile to use in bootlegging and it was seized and sold by the government, and Smith, in order to save it, bought it in at the sale, he could recover from Doe the amount he had been compelled to pay to save his property. The law regards such payments as made by compulsion. It is this rule which enables a mortgagee who, to protect his rights, pays taxes upon the mortgaged property, to recover from the owner the amount so paid. So also when Smith becomes surety for Doe

and in consequence is forced to pay Doe's debt, the law imposes upon Doe the obligation to indemnify Smith. Moreover, if Brown was also a surety for Doe for the same debt, the law lays upon Brown the obligation to contribute to Smith half the amount he paid out, so that each surety shall bear his share of the loss.

REVIEW

Distinguish between crime and tort; contract and quasi-contract. State the two elements necessary for a quasi-contractual obligation.

State what principle was brought out in the case of the Boston Ice Company vs. Potter.

Explain the law in regard to mistake as to a material fact, and mistake as to the law, from the standpoint of its effect on the rights of the parties in an agreement.

Discuss the enforceability of illegal contracts.

In cases of benefits voluntarily conferred, tell what the ruling is with regard to payment therefor.

•



INDEX

- Acceptance,**
 By mail, telegraph or telephone, 40;
 Effect of receipt of before offer re-
 lapses, 41; Of offer calling for act,
 not promise, 41; Implied in fact,
 42; Effect of in writing, 43; By
 illiterates, 43; By silence, 44;
See also Offer
- Accord,**
 Requisites of, 102
- Accounts Stated,**
 Definition of, 104; Form of, 105
- Agency,**
 Nature of, 212; Created by ex-
 press appointment, 213; Com-
 petency of parties, 213; Unin-
 corporated associations as prin-
 cipals, 214; Joint agents, 214;
 Form of appointment, 215; Writ-
 ten authorization of agent, 215;
 Seals, 215; Creation of by rati-
 fication, 216; Requisites of rati-
 fication, 216; Form of ratifica-
 tion, 218; Withdrawal before rati-
 fication, 218; Effects of ratifica-
 tion, 218; Arising by estoppel,
 219; to collect on bond and mort-
 gage from possession of docu-
 ments, 221; Termination of rela-
 tion of principal and agent, 222;
 Revocation, what constitutes, 222;
 Death of either party terminates,
 223; Irrevocable, 224
- Assignments,**
 Nature of, 93; what contractual
 rights may be assigned, 94; How
 far future contractual rights may
 be assigned, 95; Contrary to pub-
 lic policy, 96; Of executory bilat-
 eral contracts, 96; Effect of ex-
 press prohibition of consent to,
 97; Form of, 98; Distinction be-
 tween orders, checks, drafts and,
 98; Defenses of obligor against
 assignee, 99
- Auctioneers,** 240
- Auction Sales,** 25
- Bailments,**
 Nature of, 202; When bailed goods
 belong to third person 202; Gra-
- tuitous, 203; Not gratuitous, 204;
 Pledges, 205; Storage or ware-
 house, 206; With innkeepers, 207
- Bank and Depositor,**
 Relation between, 164
- Bids on Public Works,**
 Advertisements for, 25
- Bill of Lading,**
 Definition of, 171; More than a con-
 tract, 172; Fraudulent issue of,
 172
- Bills of Exchange,**
 Nature of, 146; Liability of drawee,
 147; Liability of drawer, 148;
 Rights of holder of negotiable in-
 strument, 150-152; Defenses,
 152; Incapacity, 153; Illegality,
 154; Usury, 155; Forgery, 156-
 158; Personal defenses, 158;
 Consideration, lack of, 159; Pay-
 ment, 160
- Certificate of Deposit,**
 Definition of, 173; Transferability,
 173
- Checks,**
 Nature of, 163; Rights and liability
 of drawer, 165-167; Rights and
 liability of holder, 167-169; Cer-
 tified, 169
- Common Carriers,**
 Liability of, 207; Acts of God, 208;
 Public enemies, 208; Damage due
 to character of goods shipped,
 209; Liability for delay, 209;
 Limiting liability by express con-
 tract, 209; Restricting damages
 to fixed sum, 210
- Consideration,**
 Benefit to promiser or detriment to
 promisee, 46; In unilateral con-
 tracts, 47; In bilateral contracts,
 48; Valid, 48; Contingent prom-
 ises valid, 50; A benefit to stran-
 ger, 52; Payment of full settle-
 ment of claims uncertain as to
 amount of disputed, 54; Doing
 what party is bound by law to do,
 not, 56; Past, 56
- Consideration, Valid,**
 When payment of debt is, 59

Constitutional Law, 15**Contingent Promises,**

Valid as consideration for counter-promises, 50

Contracts,

Foundation of business law, 18;

What law of includes, 18; The offer, 18-37; Types of, 19; Bilateral and unilateral, 19; Executed and executory, 20; Essentials of simple, 20; Expression of mutual assent in, 21; Without offer and acceptance, 22; Nature of offers, 22; How offers are made, 22; Preliminary agreements followed by written, 24; The acceptance, 38-45; Mistake of parties as to terms of, 44; Consideration, 46-57; Under seal, 50; In writing not under seal, 51; Special inducements to fill existing, 54; Promise to perform, 55; Validity of, 58; Infants, 58; Parties and forms, 58-70; For necessities, 59; Insane as parties to, 61; Drunkenness, 62; Married women and, 63; For benefit of third persons, 63; Third person as sole beneficiary, 64; Promisee and third person benefitted, 64; Assumption of mortgage debt, 65; When in writing, 66; Not to compete, 68; For indefinite periods, 68; Method of performance, 69; In consideration of marriage, 70; Performance, 72-92; Assignment and discharge, 93-111

Coupons,

Interest bearing, 173

Debt,

Extension of time for, 53

Delivery.

To a common carrier, 187; Of a greater or less quantity, 188; Transfer of title, 190; Reservation of title or possession by sellers, 191; Risk of loss, 192; Goods shipped under bill of lading, 192; Goods shipped C. O. D., 197

Discharge,

Of contracts, 100; Releases of contracts, 101; Cancellation and surrender, 106; Alteration, 107; By merger, 107; Impossibility of performance, 108

English Sale of Goods Act,

See Statute of Frauds

English Statute of Frauds, 182**Equity,**

Origin of, 5; Development of, 6; As supplement to law, 7

Factors,

Function of, 239

Factors Acts, 193, 239**Fiduciaries,**

Nature of relation, 327; Trust property, 329; Rights and duties of trustee, 331; Investments by trustees, 333; Trustees, other duties of, 334; Relation of third persons to trust, 335; Rights to beneficiary, 337

Fixtures,

Law of, 290

Illiterates,

Signing or acceptance of writing by, 44

Implied Trust, 328**Impossibility of Performance,**

Subjective, 108; Objective, 108; Usual method of explanation, 110

Injunction, 8**Justice,**

Definition of, 3; Difference between legal and moral, 3

Jury,

At law and in equity, 10

Law,

Nature of, 1; Object of, 3; Classifications of, 4; Distinction between legislative and judicial, 15

Law and Justice, 3**Law, Common,**

Development of, 4; Sources of, 5; Varying significance of term, 10; Of States of United States, 11; Responsiveness of, 11; Flexibility of, 11; Stability of in property and contracts, 14

Law Courts and Equity Courts,

Consideration of, 10

Law of Sales,

Principal aspects of, 178

Lawyers, 241**Leases,**

See Real Property

Legislation, 15**Letter of Credit, 173****Lunatics,**

Acts of, void, 62

Mansfield, Lord,

Doctrine of implied conditions, 82

Merchantability,

Meaning of term, 200

Money Orders, 174

Mortgages,

See Real Property

Negotiable Instruments,

Origin of, 112; Development of, 112; Negotiability, 113-115; Negotiability of promissory notes, 115; Form of, 116; Formal requisites of, 117; Written and signed by maker, 118; Unconditional promise, 119; Certainty as to amount, 120; Parties must be identified, 121; Time fixed or determinable, 121; Collateral notes, 122; Omissions and blanks, 123-125; Interest, 125; Consideration, 126; Liability of maker of note, 128; Kinds of indorsement, 129-133; Blank indorsement, 130; Special indorsement, 130; Restrictive indorsement, 131; Indorsement without recourse, 133; Conditional indorsement, 133; Liability of accommodator indorser, 134; Indorsement, other provisions, 136-138; Presentment for payment, 138; Sufficient presentment, 139-141; Dishonor, notice of, 141; Dishonor, time for notice, 143; Protest, 144

Negotiable Instrument Law,

Minors indorsement on notes, 153

Novation, 105

Offer, Gratuitous Conditional,

Distinguished from offer calling for act as consideration, 51

Offers,

Nature of, 22; How made, 22; Preliminary negotiations and advertisements, 23; By mail, 27; Indefinite, and promises, 27; Indefinite as to price, services or goods, 29; Implied from acts or conduct, 29; Termination of before acceptance, 30; Termination of by rejection, 32; Rejection of by mail or telegraph, 32; Revocation of, 33; Revocation of by advertisement, 34; Revocation of to pay for acts, 34; Termination of by death or insanity, 35; When irrevocable, 36; Acceptance of, 38; Acceptance must not modify, 39

Offers and Acceptance,

Must be communicated, 26

Parol, 24; 51

Partner,

Holding out as, 251; Power of to bind firm by contract, 261; Binding to partners under seal, 263; Selling fixed property of partnership, 264; Individual debts of, 265; Showing authority by, 266; Firm bound by wrongful act of, 267; Extent of liability, 268; Individual creditors of, 270; Final accounting to, 272

Partners,

Good faith of, 258; Application of firm assets, 259; Enforcement of obligations among, 261

Partner's Interest,

In firm property, 255

Partnership,

Legal nature of, 246; And joint ownership, 247; Forms of organization like, 249; Contract of, 250; Uniform partnership law and, 251; Sharing in profits not always, 252; Firm capital and, 253; Property of, 253; Real estate and, 254; Scope of business, 262; Rights of firm creditors, 269; Dissolution of, 271; Limited, 274

Performance,

Condition in contracts in general, 72; Express conditions of promisor, 73; Conditions implied in fact, 73; Conditions implied in law, 74; Prevented by promisor, 75; Waiver of, 76; Waiver before time for, 76; Waiver after breach of condition, 77; Conditions in sales of goods, 78; Of contract, illustrations of, 79; Conditions requiring architects certificates, 80; Conditions as to time of payment of debt, 81; Substantial, 81; Conditions implied by law in bilateral contracts, 82; Failure relieves other party from, 83; When order is not indicated, 84; Concurrent conditions, 84; Tender, readiness and willingness, 85; Impossibility of, not due to plaintiff, 86; Part or substantial, 87; Time of, 88; Contracts of sale, 89; Severable or divisible contracts, 90; Effect of prospective unwillingness or inability to perform, 91

Personal Property,

Distinguished from real property, 290; Aspects of, 316; Possession and ownership, 316; Lost property, 317; Lost chattels found on private land, 317; Misplaced chattels, 318; Adverse possession, 321; Accession, 321; Confusion, 322; Voluntary transfer of title to chattels, 323; Common Law liens on chattels, 323; Artisans' liens, 324; Warehousemen's liens, 324; General or commercial liens, 325

Principal, Agent and Third Persons,

Obligation of principal to agent, 226; Real estate brokers' commissions, 227; Effect of revocation of agency on compensation, 227; Discharge of real estate brokers, 228; Compensation where agent acts for both sides, 229; Illegal services, 230; Reimbursements and indemnity, 231; Obligations of agent to principal, 232-234; Delegation of authority by agents to others, 234; Sub-agents, 235; Liability of gratuitous agents, 236; Liability of principal to third persons, 237; General managers or general agents, 238; Agents, authority to sell, 238; Agents authority to buy, 239; Rights and liabilities of undisclosed principal, 241; Agents misrepresentation, 242; Exceptions to doctrine of undisclosed principal, 243; Notice to agent is notice to principal, 244

Quasi-Contractual Obligations,

Nature of, 240-243; When obligation arises, 243; Mistake in, 243; Mistake as to existence of contract, 244; Mistake as to identity of dealer, 245; Mistake as to subject of contract, 247; Mistake as to material fact, 248; Mistake of law, 250; Retaining benefits without making compensation, 250; Contracts void because of Statute of Frauds, 253; Benefits conferred without contract, 255

Real Property,

What it is, 289; Ownership, absolute or qualified, 292; Deeds and conveyances, 293; Deeds, differ-

ent parts of, 294; Warranty deed, covenants of title in, 295; Mortgages, 296-298; Improvements on by mortgages, 298; Rights and obligations of mortgagor, 299; Equitable mortgages, 300; Illegal mortgages, 301; Assumption of mortgage by purchaser of property, 302; Foreclosure of mortgages, 304; Leases, 307; Tenancies from year to year and month to month, 309; Tenancies at will, 311; Tenancies under void parol lease, 311; Covenants in leases, 312; Waste to, 313; Surrender of leases, 314; Possession of tenant and bailor, 319

Rescission,

By parol, 101; For breach of contract, 106

Rewards, 26**Sales,**

Contracts distinguished from work and labor contracts, 180; Acceptance and receipt of part of goods, 182; Part payment under Statute of Frauds, 183; Memorandum in writing, 184; Delivery and payment of price, 186; Examination of goods by buyer, 189; By persons without title, 193; Conditional, 193; With retention of possession by sellers, 194; Warranties, 195-200; By sample, 200; Merchantability, 200

Sales and Executory Contracts to Sell,

What they involve, 179

"Sales of Goods"

What is included in term, 181

Satisfaction,

Requisites of, 103

Satisfaction, Attempted,

Of disputed claims by check, 103

Specialties, 66**Spendthrift Trust, 328****Statute of Frauds,**

Relation to contract, 66; Origin of, 67; Application of, 67; Contracts not to be performed within a year, 68; As applied to contracts for indefinite periods, 68; Assignment of leases under, 99; Provisions of the statute, 178; Applied to sales and contracts to sell, 180; Suretyship and guarantee, 287; Applicable to land or real property, 290; Contracts void because of, 353

Statute of Limitations, 121; 351

Stock Certificates, 174-176

Suretyship and Guarantee,

What constitutes, 276; Contract between creditor and surety, 277; Defenses of debtor, effect on surety's contract, 277; Discharge of surety by payment of debt, 278; Extension of time by creditor discharges surety, 279; Reservation of right to hold surety prevents his discharge, 280; Surrender of collateral security discharges surety, 280; Variation of debtor's contract, effect of, 282; Tender of payment and rejection by creditor, 283; Failure of creditor to sue debtor, 284; Notice to surety of debtor's default, 284; Fraud or duress by debtor or creditor to surety, 284; Termination of contract, 285; Rights of surety, reimbursement, 286; Rights

of surety, contribution, 286; Contribution between sureties 287

Trade Acceptances, 176

Trustee,

See Fiduciaries

Uniform Partnership Law, 251-254; 270

Uniform Sales Act, 180; 189

Unwritten Law, 14

Warehouse Receipts, 176

Warranties,

Express, in sales, 195; Obvious defects, inspection, 195; Implied warranty of title, 196; Implied warranty of quality, 197-199; Not broken when buyer gets what he contracted for, 199; Food sold for immediate consumption by dealer is fit, 200



